

## Financial Statements of Companies

### Unit – 1: Preparation of Financial Statements

#### Learning Objectives

After studying this unit, you will be able to:

- ◆ Know how to maintain books of account of a company.
- ◆ Learn about statutory books of a company.
- ◆ Prepare and present the financial statements of a company as per Schedule III to the Companies Act, 2013 (Earlier Schedule VI to the Companies Act, 1956).
- ◆ Calculate managerial remuneration of managers in a company.
- ◆ Appreciate the term divisible profits and dividends.

**Note:** This Unit has been thoroughly revised as per relevant sections of the Companies Act, 2013 which have come into force.

### 1.1 Meaning of Company

The word 'company' derived from the Latin word '*com*' i.e. with or together and '*panis*' i.e. Bread. Originally the word referred to an association of persons or merchant men discussing matters and taking food together. In short it refers to a corporate body having perpetual succession and a common seal. As per section 2(20) of the Companies Act, 2013, "Company" means a company incorporated under this Act or under any previous company law. Different types of companies have been defined (under various sub-sections of the Companies Act, 2013) as follows:

- 2(21) "**company limited by guarantee**" means a company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake to contribute to the assets of the company in the event of its being wound up;

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- 2(22) **“Company limited by shares”** means a company having the liability of its members limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them;
- 2(42) **“Foreign company”** means any company or body corporate incorporated outside India which –
- (a) has a place of business in India whether by itself or through an agent physically or through electronic mode; and
  - (b) conducts any business activity in India in any other manner.
- 2(45) **“Government company”** means any company in which not less than fifty one per cent of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company;
- 2(62) **“One Person Company”** means a company which has only one person as a member;
- 2(68) **“Private company”** means a company having a minimum paid-up share capital of one lakh rupees or such higher paid-up share capital as may be prescribed, and which by its articles,—
- (i) restricts the right to transfer its shares;
  - (ii) except in case of One Person Company, limits the number of its members to two hundred: Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this sub-clause, be treated as a single member:  
Provided further that—
    - (A) persons who are in the employment of the company; and
    - (B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased, shall not be included in the number of members; and
  - (iii) prohibits any invitation to the public to subscribe for any securities of the company;
- 2(71) **“Public Company”** means a company which— (a) is not a private company; (b) has a minimum paid-up share capital of five lakh rupees or such higher paid-up capital, as may be prescribed: Provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the

purposes of this Act even where such subsidiary company continues to be a private company in its articles ;

- 2(85) **“Small company”** means a company, other than a public company, -
- (i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than five crore rupees; or
  - (ii) turnover of which as per its last profit and loss account does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than twenty crore rupees:

Provided that nothing in this clause shall apply to

- (A) a holding company or a subsidiary company;
  - (B) a company registered under section 8; or
  - (C) a company or body corporate governed by any special Act;
- 2(92) **“Unlimited company”** means a company not having any limit on the liability of its members;
- 2(46) **“Holding company”**, in relation to one or more other companies, means a company of which such companies are subsidiary companies;
- 2(87) **“Subsidiary company”**, or “subsidiary”, in relation to any other company (that is to say the holding company), means a company in which the holding company-
- (i) controls the composition of the Board of Directors; or
  - (ii) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies:

Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.

Explanation – For the purposes of this clause, -

- (a) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;
- (b) the composition of a company’s Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors;
- (c) the expression “company” includes any body corporate;
- (d) “layer” in relation to a holding company means its subsidiary or subsidiaries;

### 1.2 Maintenance of Books of Account

As per Section 128 of the Companies Act, 2013, Every company shall prepare and keep at its registered office books of account and other relevant books and papers and financial statement for every financial year which give a true and fair view of the state of the affairs of the company, including that of its branch office or offices, if any, and explain the transactions effected both at the registered office and its branches and such books shall be kept on accrual basis and according to the double entry system of accounting:

Provided further that the company may keep such books of account or other relevant papers in electronic mode in such manner as may be prescribed.

#### **Maintenance at Place other than Registered Office**

It is a duty of the company to inform the Registrar of Companies within seven days of the decision in case the Board of Directors decides to maintain books at the place other than the registered office.

#### **In Case of Branch Office**

Where a company has a branch office in India or outside India, it shall be deemed to have complied with the provisions of the Act, if proper books of account relating to the transactions effected at the branch office are kept at that office and proper summarised returns periodically are sent by the branch office to the company at its registered office or such other place.

Section 128 (3) further lays down that the books of account and other books and papers maintained by the company within India shall be open for inspection at the registered office of the company or at such other place in India by any director during business hours, and in the case of financial information, if any, maintained outside the country, copies of such financial information shall be maintained and produced for inspection by any director subject to such conditions as may be prescribed. Section 128(5) further states that the books of account of every company relating to a period of not less than eight financial years immediately preceding a financial year, or where the company had been in existence for a period less than eight years, in respect of all the preceding years together with the vouchers relevant to any entry in such books of account shall be kept in good order.

### 1.3 Statutory Books

The following statutory books are required to be maintained by a company under different sections of the Companies Act, 2013:

- ◆ Register of Investments of the company held in its own name (Section 187).
- ◆ Register of Charges (Section 85).
- ◆ Register of Members (Sections 88).
- ◆ Register of Debenture-holders and other Security holders (Section 88).

- ◆ Minute Books (Section 118).
- ◆ Register of Contracts, or arrangements in which directors are interested (Section 189).
- ◆ Register of directors and key managerial personnels and their shareholding (Section 170).
- ◆ Register of Loans to Directors etc. (Section 185)
- ◆ Register of Loans and Investments by Company (Section 186).

In addition, a company usually maintains a number of statistical books to keep a record of its transactions which have resulted either in the payment of money to it or constitute the basis on which certain payments have been made by it.

- ◆ Registers and documents relating to the issue of shares are:
  - (i) Share Application and Allotment Book;
  - (ii) Share Call Book; and
  - (iii) Certificate Book.
  - (iv) Register of Members
  - (v) Share Transfer Book
  - (vi) Dividend Register

#### 1.4 Annual Return

- (1) Section Applicable  
Section 92 of the Companies Act, 2013.
- (2) Number of Days  
Within 60 days from the day on which each of the annual general meeting (AGM) is held or where no AGM is held in any year, within 60 days from the date on which AGM should have been held along with a statement showing the reasons why AGM was not held.
- (3) Documents to be filed  
Prepare and file with the Registrar the annual return containing the particulars specified under Section 92 of the Act.
- (4) Form Applicable  
The annual return shall be in the Form prescribed by the Companies Act, 2013.

#### 1.5 Final Accounts

Under Section 129 of the Companies Act, 2013, at the annual general meeting of a company, the Board of Directors of the company shall lay financial statements before the company:

Financial Statements as per Section 2(40) of the Companies Act, 2013, inter-alia include -

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- (i) a balance sheet as at the end of the financial year;
- (ii) a profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year;
- (iii) cash flow statement for the financial year;
- (iv) a statement of changes in equity, if applicable; and
- (v) any explanatory note annexed to, or forming part of, any document referred to in sub-clause (i) to sub-clause (iv):

Provided that the financial statement, with respect to One Person Company, small company and dormant company, may not include the cash flow statement.

### Requisites of Financial Statements

It shall give a true and fair view of the state of affairs of the company as at the end of the financial year.

### Provisions Applicable

- (1) Specific Act is Applicable

For instance any

- (a) insurance company
- (b) banking company or
- (c) any company engaged in generation or supply of electricity\* or
- (d) any other class of company for which a Form of balance sheet or Profit and loss account has been prescribed under the Act governing such class of company

- (2) In case of all other companies

Balance Sheet as per Form set out in Part I of Schedule III and Statement of Profit and Loss as per Part II of Schedule III

### Points to be kept in mind while preparing final accounts:

- ◆ Requirements of Schedule III to the Companies Act;
- ◆ Other statutory requirements;
- ◆ Accounting Standards issued by the Institute of Chartered Accountants of India on different accounting matters and notified by the Central Government (AS 1 to AS 32);

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\* The Electricity Act, 2003 does not specify any format for presentation of Financial Statements. Therefore, Schedule III of the Companies Act, 2013 is followed by Electricity Companies in preparation of their financial statements.

- ◆ Statements and Guidance Notes issued by the Institute of Chartered Accountants of India; which are necessary for understanding the accounting treatment / valuation / disclosure suggested by the ICAI.

### **Compliance with Accounting Standards**

As per section 133 of the Companies Act, it is mandatory to comply with accounting standards notified by the Central Government from time to time.

### **Schedule III of the Companies Act, 2013**

As per section 129 of the Companies Act, 2013, Financial statements shall give a true and fair view of the state of affairs of the company or companies and comply with the accounting standards notified under section 133 and shall be in the form or forms as may be provided for different class or classes of companies in Schedule III under the Act. Schedule III to the Companies Act, 2013 has been given as Appendix II at the end of the Module I of the Study Material. For full details please verify Appendix II of the Module I of the study material.

### **Example 1**

*In the financial statements of the financial year 2014-15, Alpha Ltd. has mentioned in the notes to accounts that during financial year, 24,000 equity shares of ₹ 10 each were issued as fully paid bonus shares. However, the source from which these bonus shares were issued has not been disclosed. Is such non-disclosure a violation of the Schedule III to the Companies Act? Comment.*

### **Solution**

Schedule III has come into force for the Balance Sheet and Profit and Loss Account prepared for the financial year commencing on or after 1<sup>st</sup> April, 2014. As per Part I of the Schedule III, a company shall, inter alia, disclose in notes to accounts for the period of 5 years immediately preceding the balance sheet date (31<sup>st</sup> March, 2015 in the instant case) the aggregate number and class of shares allotted as fully paid-up bonus shares. Schedule III does not require a company to disclose the source from which bonus shares have been issued. Therefore, non-disclosure of source from which bonus shares have been issued does not violate the Schedule III to the Companies Act.

### **Example 2**

The management of Loyal Ltd. contends that the work in process is not valued since it is difficult to ascertain the same in view of the multiple processes involved. They opine that the value of opening and closing work in process would be more or less the same. Accordingly, the management had not separately disclosed work in process in its financial statements. Comment in line with Schedule III.

### Solution

Schedule III to the companies Act does not require that the amounts for which WIP have been completed at the beginning and at the end of the accounting period should be disclosed in the statement of profit and loss. Therefore, the non-disclosure in the financial statements by the company may not amount to violation of Schedule III if the differences between opening and closing WIP are not material.

**Note:** Students may note that the questions based on preparation of Statement of Profit and Loss, Balance Sheet (including statement of changes in equity) and explanatory notes as per Schedule III have been given in this Unit. However, questions requiring preparation of cash Flow statements have been separately given in the next unit of this chapter.

## 1.6 Managerial Remuneration

Managerial remuneration is calculated as a percentage on profit. Managerial remuneration payable by a company is governed by various sections of the Companies Act, 2013 and also schedule V under the Companies Act, 2013.

The scope of the relevant sections is as below:

Section 197 prescribes the overall maximum managerial remuneration payable and also managerial remuneration in case of absence or inadequacy of profits.

As per Section 197 of the Companies Act, 2013, total managerial remuneration payable by a public company, to its directors, including managing director and whole-time director, and its manager in respect of any financial year shall not exceed eleven per cent of the net profits of that company for that financial year computed in the manner laid down in section 198 except that the remuneration of the directors shall not be deducted from the gross profits: provided that the company in general meeting may, with the approval of the Central Government, authorize the payment of remuneration exceeding eleven per cent. of the net profits of the company, subject to the provisions of Schedule V.

Provided further that, except with the approval of the company in general meeting,—

- (i) the remuneration payable to any one managing director; or whole-time director or manager shall not exceed five per cent. of the net profits of the company and if there is more than one such director remuneration shall not exceed ten per cent of the net profits to all such directors and manager taken together;
- (ii) the remuneration payable to directors who are neither managing directors nor whole-time directors shall not exceed,—
  - (A) one per cent of the net profits of the company, if there is a managing or whole-time director or manager;



(B) three per cent of the net profits in any other case.

Section 198 lays down how the net profit of the company will be ascertained for the purpose of calculating managerial remuneration.

Schedule V consists of four parts. Part I lays down conditions to be fulfilled for the appointment of a managing or whole-time director or a manager without the approval of the Central Government. Part II deals with remuneration payable to managerial person by companies having profits and also by companies having no profits or inadequate profits. Part III specifies the provisions applicable to parts 1 and 2 of this schedule and Part IV deals with Central Government's power to relax any rules.

The relevant details given under Part II of Schedule V are as follows:

**Section I - Remuneration payable by companies having profits:**

Subject to the provisions of section 197, a company having profits in a financial year may pay remuneration to a managerial person or persons not exceeding the limits specified in such section.

**Section II - Remuneration payable by companies having no profit or inadequate profit without Central Government approval:**

Where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may, without Central Government approval, pay remuneration to the managerial person not exceeding the higher of the limits under (A) and (B) given below:-

	(1)	(2)
	<i>Where the effective capital* is</i>	<i>Limit of yearly remuneration payable shall not exceed (Rupees)</i>
(i)	Negative or less than 5 crores	30 lakhs
(ii)	5 crores and above but less than 100 crores	42 lakhs
(iii)	100 crores and above but less than 250 crores	60 lakhs
(iv)	250 crores and above	60 lakhs plus 0.01% of the effective capital in excess of ₹ 250 crores.

Provided that the above limits shall be doubled if the resolution passed by the shareholders is a special resolution.

*Explanation* - It is hereby clarified that for a period less than one year, the limits shall be pro-rated.

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*\*Effective Capital has been explained after Section IV in the succeeding pages of this unit. Students are advised to please refer that definition of Effective Capital.*

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(B) In the case of a managerial person who was not a security holder holding securities of the company of nominal value of rupees five lakh or more or an employee or a director of the company or not related to any director or promoter at any time during the two years prior to his appointment as a managerial person, - 2.5% of the current relevant profit:

Provided that if the resolution passed by the shareholders is a special resolution, this limit shall be doubled:

Provided further that the limits specified under this section shall apply, if-

- (i) payment of remuneration is approved by a resolution passed by the Board and, in the case of a company covered under sub-section (1) of section 178 also 'by the Nomination and Remuneration Committee;
- (ii) the company has not made any default in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of thirty days in the preceding financial year before the date of appointment of such managerial person;
- (iii) a special resolution has been passed at the general meeting of the company for payment of remuneration for a period not exceeding three years;
- (iv) a statement along with a notice calling the general meeting referred to in clause (iii) is given to the shareholders containing the following information, namely:-
  - I. General Information:
    - (1) Nature of industry
    - (2) Date or expected date of commencement of commercial production.
    - (3) In case of new companies, expected date of commencement of activities as per project approved by financial institutions appearing in the prospectus
    - (4) Financial performance based on given indicators
    - (5) Foreign investments or collaborations, if any.
  - II. Information about the appointee:
    - (1) Background details
    - (2) Past remuneration
    - (3) Recognition or awards
    - (4) Job profile and his suitability
    - (5) Remuneration proposed
    - (6) Comparative remuneration profile with respect to industry, size of the company, profile of the position and person (in case of expatriates the relevant details would be with respect to the country of his origin)

- (7) Pecuniary relationship directly or indirectly with the company, or relationship with the managerial personnel, if any.

III. Other information:

- (1) Reasons of loss or inadequate profits
- (2) Steps taken or proposed to be taken for improvement
- (3) Expected increase in productivity and profits in measurable terms.

IV. Disclosures:

The following disclosures shall be mentioned in the Board of Director's report under the heading "Corporate Governance", if any, attached to the financial statement:-

- (i) all elements of remuneration package such as salary, benefits, bonuses, stock options, pension, etc., of all the directors;
- (ii) details of fixed component and performance linked incentives along with the performance criteria;
- (iii) service contracts, notice period, severance fees;
- (iv) stock option details, if any, and whether the same has been issued at a discount as well as the period over which accrued and over which exercisable.

**Section III - Remuneration payable by companies having no profit or inadequate profit without Central Government approval in certain special circumstances**

In the following circumstances a company may, without the Central Government approval, pay remuneration to a managerial person in excess of the amounts provided in Section II above:-

- (a) where the remuneration in excess of the limits specified in Section I or II is paid by any other company and that other company is either a foreign company or has got the approval of its shareholders in general meeting to make such payment, and treats this amount as managerial remuneration for the purpose of section 197 and the total managerial remuneration payable by such other company to its managerial persons including such amount or amounts is within permissible limits under section 197.
- (b) where the company-
  - (i) is a newly incorporated company, for a period of seven years from the date of its incorporation, or
  - (ii) is a sick company, for whom a scheme of revival or rehabilitation has been ordered by the Board for Industrial and Financial Reconstruction or National Company Law Tribunal, for a period of five years from the date of sanction of scheme of revival, it may pay remuneration up to two times the amount permissible under Section II.

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- (c) where remuneration of a managerial person exceeds the limits in Section II but the remuneration has been fixed by the Board for Industrial and Financial Reconstruction or the National Company Law Tribunal:

Provided that the limits under this Section shall be applicable subject to meeting all the conditions specified under Section II and the following additional conditions:-

- (i) except as provided in para (a) of this Section, the managerial person is not receiving remuneration from any other company;
  - (ii) the auditor or Company Secretary of the company or where the company has not appointed a Secretary, a Secretary in whole-time practice, certifies that all secured creditors and term lenders have stated in writing that they have no objection for the appointment of the managerial person as well as the quantum of remuneration and such certificate is filed along with the return as prescribed under sub-section (4) of section 196.
  - (iii) the auditor or Company Secretary or where the company has not appointed a secretary, a secretary in whole-time practice certifies that there, is no default on payments to any creditors, and all dues to deposit holders are being settled on time.
- (d) a company in a Special Economic Zone as notified by Department of Commerce from time to time which has not raised any money by public issue of shares or debentures in India, and has not made any default in India in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of thirty days in any financial year, may pay remuneration up to ₹2,40,00,000 per annum.

### **Section IV -Perquisites not included in managerial remuneration:**

1. A managerial person shall be eligible for the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in Section II and Section III:-
  - (a) contribution to provident fund, superannuation fund or annuity fund to the extent these either singly or put together are not taxable under the Income-tax Act, 1961;
  - (b) gratuity payable at a rate not exceeding half a month's salary for each completed year of service; and
  - (c) encashment of leave at the end of the tenure.
2. In addition to the perquisites specified in paragraph 1 of this section, an expatriate managerial person (including a non-resident Indian) shall be eligible to the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in Section II or Section III-

- (a) Children's education allowance: In case of children studying in or outside India, an allowance limited to a maximum of ₹12,000 per month per child or actual expenses incurred, whichever is less. Such allowance is admissible up to a maximum of two children.
- (b) Holiday passage for children studying outside India or family staying abroad: Return holiday passage once in a year by economy class or once in two years by first class to children and to the members 'of the family from the place of their study or stay abroad to India if they are not residing in India, with the managerial person.
- (c) Leave travel concession: Return passage for self and family in accordance with the rules specified by the company where it is proposed that the leave be spent in home country instead of anywhere in India.

Explanation I - For the purposes of Section II of this Part, "**Effective capital**" means the aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account; reserves and surplus (excluding revaluation reserve); long-term loans and deposits repayable after one year (excluding working capital loans, over drafts, interest due on loans unless funded, bank guarantee, etc., and other short-term arrangements) as reduced by the aggregate of any investments (except in case of investment by an investment company whose principal business is acquisition of shares, stock, debentures or other securities), accumulated losses and preliminary expenses not written off.

Explanation II - (a) Where the appointment of the managerial person is made in the year in which company has been incorporated, the effective capital shall be calculated as on the date of such appointment;

(b) In any other case the effective capital shall be calculated as on the last date of the financial year preceding the financial year in which the appointment of the managerial person is made.

Explanation III - For the purposes of this Schedule, "family" means the spouse, dependent children and dependent parents of the managerial person.

Explanation IV - The Nomination and Remuneration. Committee while approving the remuneration under Section II or Section III, shall -

- (a) take into account, financial position of the company, trend in the industry, appointee's qualification, experience, past performance, past remuneration, etc.;
- (b) be in a position to bring about objectivity in determining the remuneration package while striking a balance between the interest of the company and the shareholders.

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Explanation V – For the purposes of this Schedule, "negative effective capital" means the effective capital which is calculated in accordance with the provisions contained in Explanation I of this Part is less than zero.

Explanation VI - For the purposes of this Schedule:-

(A) "current relevant profit" means the profit as calculated under section 198 but without deducting the excess of expenditure over income referred to in sub-section 4 (I) thereof in respect of those years during which the managerial person was not an employee, director or shareholder of the company or its holding or subsidiary companies.

(B) "Remuneration" means remuneration as defined in clause 78 of section 2 and includes reimbursement of any direct taxes to the managerial person.

### **Section V - Remuneration payable to a managerial person in two companies:**

Subject to the provisions of sections I to IV, a managerial person shall draw remuneration from one or both companies, provided that the total remuneration drawn from the companies does not exceed the higher maximum limit admissible from anyone of the companies of which he is a managerial person.

Note: The appointment and remuneration referred to in Part I and Part II of this Schedule shall be subject to approval by a resolution of the shareholders in general meeting.

### **Ascertainment of profit for managerial remuneration**

As we have seen above that in case of a company having profits, managerial remuneration is calculated as a percentage on net profit. Such net profit is to be arrived in accordance with the provisions of Section 198 of the Companies Act, 2013.

As per Section 198 of the Companies Act, 2013,

- (I) In making the computation aforesaid, credit shall be given for the bounties and subsidies received from any Government, or any public authority constituted or authorised in this behalf, by any Government, unless and except in so far as the Central Government otherwise directs. In making the computation of the net profits, credit shall not be given for the following sums, namely:—
- (a) profits, by way of premium on shares or debentures of the company, which are issued or sold by the company;
  - (b) profits on sales by the company of forfeited shares;
  - (c) profits of a capital nature including profits from the sale of the undertaking or any of the undertakings of the company or of any part thereof;
  - (d) profits from the sale of any immovable property or fixed assets of a capital nature comprised in the undertaking or any of the undertakings of the company, unless the business of the company consists, whether wholly or partly, of buying and selling any such property or assets: Provided that where the amount for which any fixed

asset is sold exceeds the written-down value thereof, credit shall be given for so much of the excess as is not higher than the difference between the original cost of that fixed asset and its written-down value;

- (e) any change in carrying amount of an asset or of a liability recognised in equity reserves including surplus in profit and loss account on measurement of the asset or the liability at fair value.
- (II) In making the computation aforesaid, the following sums shall be deducted, namely:—
- (a) all the usual working charges;
  - (b) directors' remuneration;
  - (c) bonus or commission paid or payable to any member of the company's staff, or to any engineer, technician or person employed or engaged by the company, whether on a whole-time or on a part-time basis;
  - (d) any tax notified by the Central Government as being in the nature of a tax on excess or abnormal profits;
  - (e) any tax on business profits imposed for special reasons or in special circumstances and notified by the Central Government in this behalf;
  - (f) interest on debentures issued by the company;
  - (g) interest on mortgages executed by the company and on loans and advances secured by a charge on its fixed or floating assets;
  - (h) interest on unsecured loans and advances;
  - (i) expenses on repairs, whether to immovable or to movable property, provided the repairs are not of a capital nature;
  - (j) outgoings inclusive of contributions made under section 181 of the Act;
  - (k) depreciation to the extent specified in section 123 of the Act;
  - (l) the excess of expenditure over income, which had arisen in computing the net profits in accordance with this section in any year which begins at or after the commencement of this Act, in so far as such excess has not been deducted in any subsequent year preceding the year in respect of which the net profits have to be ascertained;
  - (m) any compensation or damages to be paid in virtue of any legal liability including a liability arising from a breach of contract;
  - (n) any sum paid by way of insurance against the risk of meeting any liability such as is referred to in clause (m);
  - (o) debts considered bad and written off or adjusted during the year of account.

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(III) In making the computation aforesaid, the following sums shall not be deducted, namely:—

- (a) income-tax and super-tax payable by the company under the Income-tax Act, 1961, or any other tax on the income of the company not falling under clauses (d) and (e) of sub-section (4);
- (b) any compensation, damages or payments made voluntarily, that is to say, otherwise than in virtue of a liability such as is referred to in clause (m) of sub-section (4);
- (c) loss of a capital nature including loss on sale of the undertaking or any of the undertakings of the company or of any part thereof not including any excess of the written-down value of any asset which is sold, discarded, demolished or destroyed over its sale proceeds or its scrap value;
- (d) any change in carrying amount of an asset or of a liability recognised in equity reserves including surplus in profit and loss account on measurement of the asset or the liability at fair value.

### Example 3

The following is the Draft Profit & Loss A/c of Mudra Ltd., the year ended 31st March, 2015:

₹		₹	
To	Administrative, Selling and distribution expenses	By	Balance b/d
	8,22,542		5,72,350
			“ Balance from Trading A/c
			40,25,365
			“ Subsidies received from Govt.
			2,73,925
”	Directors fees		1,34,780
”	Interest on debentures		31,240
”	Managerial remuneration		2,85,350
”	Depreciation on fixed assets		5,22,543
”	Provision for Taxation		12,42,500
”	General Reserve		4,00,000
”	Investment Revaluation Reserve		12,500
”	Balance c/d		14,20,185
			<u>48,71,640</u>
			<u>48,71,640</u>

Depreciation on fixed assets as per Schedule II of the Companies Act, 2013 was ₹5,75,345. You are required to calculate the maximum limits of the managerial remuneration as per Companies Act, 2013.

**Solution:**

### Calculation of net profit u/s 198 of the Companies Act, 2013

₹		₹	
Balance from Trading A/c			40,25,365



Add : Subsidies received from Government		<u>2,73,925</u>
		42,99,290
Less : Administrative, selling and distribution expenses	8,22,542	
Director's fees	1,34,780	
Interest on debentures	31,240	
Depreciation on fixed assets as per Schedule II	<u>5,75,345</u>	<u>(15,63,907)</u>
Profit u/s 198		<u>27,35,383</u>

Maximum Managerial remuneration under Companies Act, 2013 = 11% of ₹ 27,35,383 = ₹3,00,892

#### Example 4

The following extract of Balance Sheet of X Ltd. was obtained:

#### Balance Sheet (Extract) as on 31st March, 2015

Liabilities	₹
Authorised capital:	
20,000, 14% preference shares of ₹100	20,00,000
2,00,000 Equity shares of ₹100 each	<u>2,00,00,000</u>
	<u>2,20,00,000</u>
Issued and subscribed capital:	
15,000, 14% preference shares of ₹ 100 each fully paid	15,00,000
1,20,000 Equity shares of ₹ 100 each, ₹ 80 paid-up	96,00,000
Share suspense account	20,00,000
Reserves and surplus	
Capital reserves (₹ 1,50,000 is revaluation reserve)	1,95,000
Securities premium	50,000
Secured loans:	
15% Debentures	65,00,000
Unsecured loans:	
Public deposits	3,70,000
Cash credit loan from SBI (short term )	4,65,000
Current Liabilities:	
Trade Payables	<u>3,45,000</u>
Assets:	
Investment in shares, debentures, etc.	75,00,000
Profit and Loss account (Dr. balance)	15,25,000
Share suspense account represents application money received on shares, the allotment of which is not yet made.	

## 2.18 Accounting

You are required to compute effective capital as per the provisions of Schedule V. Would your answer differ if X Ltd. is an investment company?

### Solution

Computation of effective capital :

	Where X Ltd. is a non-investment company ₹	Where X Ltd. is an investment company ₹
Paid-up share capital —		
15,000, 14% Preference shares	15,00,000	15,00,000
1,20,000 Equity shares	96,00,000	96,00,000
Capital reserves	45,000	45,000
Securities premium	50,000	50,000
15% Debentures	65,00,000	65,00,000
Public Deposits	<u>3,70,000</u>	<u>3,70,000</u>
(A)	<u>1,80,65,000</u>	<u>1,80,65,000</u>
Investments	75,00,000	—
Profit and Loss account (Dr. balance)	<u>15,25,000</u>	<u>15,25,000</u>
(B)	<u>90,25,000</u>	<u>15,25,000</u>
Effective capital (A–B)	<u>90,40,000</u>	<u>1,65,40,000</u>

## 1.7 Divisible Profit

One of the important functions of company accounting is to determine the amount of profits which is available for distribution to the shareholders as dividend. This is necessary since the amount of profits disclosed by the Profit & Loss Account, in every case, is not available for distribution. The availability of profits for distribution depends on a number of factors, e.g., their composition, the amount of provisions and appropriations that must be made out of them in priority, etc.

### Meaning of Dividend

- A dividend is a distribution of divisible profit of a company among the members according to the number of shares held by each of them in the capital of the company and the rights attaching thereto.
- Such a distribution may or may not entail a release of assets; it would be where a distribution involves payment of cash.

- (c) But when profits are capitalised and the amount distributed is applied towards payment of bonus shares, issued free to the share holders, no part of the assets of the company can be said to have been released since, in such a case, profits are only capitalised, thereby increasing the paid up capital of the company. The company does not give up any asset.

As per Section 2 (35) of the Companies Act, 2013, term "Dividend" includes interim dividend also.

Under Section 123 (1) of the Companies Act, 2013, no dividend shall be declared or paid by a company for any financial year except-

- (a) Out of the profits of the company for that financial year arrived at after providing for depreciation in accordance with the provisions of section 123(2), or
- (b) Out of the profits for any previous financial years arrived at after providing for depreciation in accordance with the provisions of that sub section and remaining undistributed; or
- (c) Out of both the above;
- (d) Out of the moneys provided by the Central Government or any State Government for the payment of dividend by the Company in pursuance of any guarantee given by that government

Provided that no dividend shall be declared or paid by a company from its reserves other than free reserves.

Declaration of a dividend presupposes that there is a trading profit or a surplus available for distribution, arrived at after providing for depreciation on assets, not only for the year in which the profits were earned but also for any arrears of depreciation of the past years, calculated in the manner prescribed by sub-section (2) of Section 123.

Sub-section (3) of Section 124 further states that the Board of Directors of a company may declare interim dividend during any financial year out of the surplus in the profit and loss account and out of profits of the financial year in which such interim dividend is sought to be declared: Provided that in case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.

***Dividends cannot be declared except out of profits.***

***Capital cannot be returned to the shareholders by way of dividend.***

Dividend can be declared and paid by a company only out of the profits or free reserves (other than moneys provided by Central or State Govt.) as the payment of dividend from any other source will amount to payment of dividend from capital units.

### **Provision for Depreciation**

Section 123(2) provides that depreciation must be to the extent specified in Schedule II to the Companies Act, 2013. Further, when the assets are sold, discarded, demolished or destroyed in any financial year, the excess of the written down value over its sale proceeds as scrap, if any should be written off in the same financial year.

### **Declaration and Payment of Dividend**

For the purpose of second proviso to sub-section (1) of section 123, a company may declare dividend out of the accumulated profits earned by it in previous years and transferred by it to the reserves, in the event of inadequacy or absence of profits in any year, subject to the fulfillment of the following conditions as per Companies (Declaration and Payment of Dividend) Rules, 2014

- (1) The rate of dividend declared shall not exceed the average of the rates at which dividend was declared by it in the three years immediately preceding that year: provided that this sub-rule shall not apply to a company, which has not declared any dividend in each of the three preceding financial year.
- (2) The total amount to be drawn from such accumulated profits shall not exceed one-tenth of the sum of its paid-up share capital and free reserves as appearing in the latest audited financial statement.
- (3) The amount so drawn shall first be utilised to set off the losses incurred in the financial year in which dividend is declared before any dividend in respect of equity shares is declared.
- (4) The balance of reserves after such withdrawal shall not fall below fifteen per cent of its paid up share capital as appearing in the latest audited financial statement.
- (5) No company shall declare dividend unless carried over previous losses and depreciation not provided in previous year are set off against profit of the company of the current year the loss or depreciation, whichever is less, in previous years is set off against the profit of the company for the year for which dividend is declared or paid.

### **Transfer to Reserves**

- I     The Board of Directors are free and can appropriate a part of the profits to the credit of a reserve or reserves as per section 123 (1) of the Companies Act, 2013.
- II    Appropriation of a part of profit is sometimes made under law.
  - (a) For example, under the Banking Regulation Act, a fixed percentage of the profit of a banking company must first be transferred to the General Reserve before any dividend can be distributed.

- (b) Transfer of a part of profit to a reserve is also necessary where the company has undertaken, at the time of raising of loan, that before any part of its profit is distributed, a specified percentage of the profit every year shall be credited to a reserve for the repayment of the loan and until the time for repayment arrives, the amount shall remain invested in a specified manner.
- III Apart from appropriations aforementioned, it may also be necessary to provide for losses and arrears of depreciation and to exclude capital profit, as mentioned earlier, to arrive at the amount of divisible profit.

**Meaning of Capital reserve**

- (a) It is the reserve which does not include any amount regarded as free for distribution through the Profit and Loss account.
- (b) Securities Premium and Capital Redemption Reserve Account should not be credited to capital reserve; these accounts have to be kept separate.
- (c) Only profits or a surplus of a capital nature can be credited to such a reserve.

The following are instances of profit or surpluses which can be so credited:

1. Profit prior to incorporation.
2. Capital profit on sale of fixed assets when these are not available for distribution as dividends in the circumstances mentioned below :
  - (i) Where the profit on sale of a fixed asset has not been realised; or
  - (ii) Where the profit on sale of fixed assets though realised is likely to be wiped out by the deficiency on revaluation of other assets; or
  - (iii) Where the Articles of Association do not permit distribution of such profit as a dividend.
3. The excess of the value of net assets over the price paid for the acquisition of a business.
4. Profit on re-issue of forfeited shares.
5. The credit balance in the Capital Reduction Account, where there has been a reduction of capital with the consent of the Court.

**Declaration of Dividend**

As per Section 123 of the Companies Act, 2013, Board of Directors of a company may declare dividend including interim dividend during any financial year out of the surplus in the profit and loss account and out of profits of the financial year in which such interim dividend is sought to be declared:

Provided that in case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such

## **2.22 Accounting**

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interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.

The amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate account within five days from the date of declaration of such dividend.

No dividend shall be paid by a company in respect of any share therein except to the registered shareholder of such share or to his order or to his banker and shall not be payable except in cash: Provided that nothing in Section 123 shall be deemed to prohibit the capitalisation of profits or reserves of a company for the purpose of issuing fully paid-up bonus shares or paying up any amount for the time being unpaid on any shares held by the members of the company:

Provided further that any dividend payable in cash may be paid by cheque or warrant or in any electronic mode to the shareholder entitled to the payment of the dividend.

### **Dividend on preference shares**

- (a) Holders of preference shares are entitled to receive a dividend at a fixed rate before any dividend is declared on equity shares.
- (b) But such a right can be exercised subject to there being profits and the Directors recommending payment of the dividend.

### **Dividend on partly paid shares:**

- (a) Provision in Articles
  - In the case of partly paid-up shares, the dividend is payable either on the nominal, called up or the paid-up amount of shares, depending on the provision in this regard that there may be in the Articles.
  - A company may if so authorised by its Article, pay a dividend in proportion to the amount paid on each share, where a larger amount is paid on some share than on other (Section 51 of the Companies Act, 2013).
- (b) No Such Provision
  - In such a case the amount of dividend payable will be calculated on the amount paid up on shares, and while doing so, the dates on which the amounts were paid must be taken into account.
  - Amount of dividend payment will have to be calculated on nominal amount of shares.
  - Dividends are to be declared and paid according to the amounts paid or credited as paid on the shares in respect whereof the dividend, is paid but, if and so long as nothing is paid upon any of the shares in the company, dividends may be declared and paid according to the nominal amounts of the shares.

- In the case of fresh issue of capital, the holders thereof, unless precluded by the terms of issue, are entitled to receive dividend *pari passu* with the shares already issued.

### **Calls in Advance**

Calls paid in advance do not rank for payment of dividend.

### **Payment of Dividend\***

As per Section 124 of the Companies Act, 2013:

- (1) Where a dividend has been declared by a company but has not been paid or claimed within thirty days from the date of the declaration to any shareholder entitled to the payment of the dividend, the company shall, within seven days from the date of expiry of the said period of thirty days, transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in that behalf in any scheduled bank to be called the Unpaid Dividend Account.
- (2) The company shall, within a period of ninety days of making any transfer of an amount under this section to the Unpaid Dividend Account, prepare a statement containing the names, their last known addresses and the unpaid dividend to be paid to each person and place it on the website of the company, if any, and also on any other website approved by the Central Government for this purpose, in such form, manner and other particulars as may be prescribed.
- (3) If any default is made in transferring the total amount or any part thereof to the Unpaid Dividend Account of the company, it shall pay, from the date of such default, interest on so much of the amount as has not been transferred to the said account, at the rate of twelve per cent per annum and the interest accruing on such amount shall enure to the benefit of the members of the company in proportion to the amount remaining unpaid to them.
- (4) Any person claiming to be entitled to any money transferred to the Unpaid Dividend Account of the company may apply to the company for payment of the money claimed.
- (5) Any money transferred to the Unpaid Dividend Account of a company in pursuance of this section which remains unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred by the company along with interest accrued, if any, thereon to the Fund "Investor Education and Protection Fund" established section 125 and the company shall send a statement in the prescribed form of the details of such transfer to the authority which administers the said Fund and that authority shall issue a receipt to the company as evidence of such transfer.

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\* It may be noted that section 124 and section 125 have not been notified till 31<sup>st</sup> May, 2015.

## 2.24 Accounting

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- (6) All shares in respect of which unpaid or unclaimed dividend has been transferred to "Investor Education and Protection Fund" shall also be transferred by the company in the name of Investor Education and Protection Fund along with a statement containing such details as may be prescribed:

Provided that any claimant of shares transferred above shall be entitled to claim the transfer of shares from Investor Education and Protection Fund in accordance with such procedure and on submission of such documents as may be prescribed.

- (7) If a company fails to comply with any of the requirements of this section, the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

### Example 5

Due to inadequacy of profits during the year ended 31<sup>st</sup> March, 2015, XYZ Ltd. proposes to declare 10% dividend out of general reserves. From the following particulars, ascertain the amount that can be utilized from general reserves, according to the Companies (Declaration of dividend out of Reserves) Rules, 2014:

	₹
17,500 9% Preference shares of ₹ 100 each, fully paid up	17,50,000
8,00,000 Equity shares of ₹ 10 each, fully paid up	80,00,000
General Reserves as on 1.4.2014	25,00,000
Capital Reserves as on 1.4.2014	3,00,000
Revaluation Reserves as on 1.4.2014	3,50,000
Net profit for the year ended 31 <sup>st</sup> March, 2015	3,00,000
Average rate of dividend during the last five year has been 12%.	

### Solution

Amount that can be drawn from reserves for 10% dividend

10% dividend on ₹ 80,00,000	₹ 8,00,000
Profits available	
Current year profit	3,00,000
Less: Preference dividend	(1,57,500)
Amount which can be utilized from reserves	<u>6,57,500</u>

Conditions as per Companies (Declaration of dividend out of Reserves) Rules, 2014:



*Condition I*

Since 10% is lower than the average rate of dividend (12%), 10% dividend can be declared.

*Condition II*

Maximum amount that can be drawn from the accumulated profits and reserves should not exceed 10% of paid up capital plus free reserves ie. ₹ 12,25,000 [10% of (80,00,000+17,50,000+25,00,000)]

*Condition III*

The balance of reserves after drawl ₹18,42,500 (₹ 25,00,000 - ₹ 6,57,500) shall not fall below 15 % of its paid up capital ie. ₹ 14,62,500 (15% of ₹ 97,50,000]

Since all the three conditions are satisfied, the company can withdraw ₹ 6,57,500 from accumulated reserves.(as per Declaration and Payment of Dividend Rules, 2014.)

**Dividend Distribution Tax****1. Meaning**

- (a) The Finance Act, 1997, has introduced Chapter XIID (Sections 115O and 115Q) on "Special Provisions Relating to Tax on Distributed profits of Domestic Companies" [Hereinafter referred to as 'DDT' (Dividend Distribution tax)]. The ICAI has also issued Guidance Note on Accounting for Corporate Dividend Tax.
- (b) The salient features of DDT are as below:
  - (i) DDT is in addition to the income-tax chargeable in respect of the total income of a domestic company.
  - (ii) ***With effect from 1<sup>st</sup> Oct, 2014 dividend and income distribution tax is leviable on gross dividend / income and not on the net dividend / income distributed to shareholders and unit holders as per Income- tax Act, 1961.***
  - (iii) The dividends chargeable to DDT may be out of the current profits or accumulated profits.
  - (iv) ***The rate of DDT is fifteen per cent (excluding surcharge of 12% plus secondary and higher education cess is (2+1) 3%).***
  - (v) DDT shall be payable even if no income-tax is payable by the domestic company on its total income.
  - (vi) DDT is payable to the credit of the Central Government within 14 days of
    - (a) declaration of any dividend,
    - (b) distribution of any dividend, or
    - (c) payment of any dividend.

## 2.26 Accounting

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whichever is the earliest.

(vii) DDT paid shall be treated as the final payment of tax on the dividends and no further credit therefore shall be claimed by the company or by any person in respect of the tax so paid.

(viii) The expression 'dividend' shall have the same meaning as is given to 'dividend' in Section 2 of the Companies Act, 2013.

**To make clear the understanding of the concept of grossing for calculation of CDT, an example has been given as follows:**

### **Example**

**X Ltd., a domestic company, has distributed on 5<sup>th</sup> April 2015, dividend of ₹ 230 lakh to its shareholders. Compute the Dividend Distribution tax payable by X Ltd.**

### **Solution**

#### **Calculation of corporate dividend tax**

<b>Particulars</b>	<b>₹ in lakh</b>
<b>Dividend distributed by X Ltd.</b>	<b>230</b>
<b>Add: Increase for the purpose of grossing up of dividend</b> $\left[ \frac{15}{100 - 15} \times 230 \right]$	<b><u>40.58</u></b>
<b>Gross dividend</b>	<b><u>270.59</u></b>
<b>Dividend distribution tax @ 15% [15% of ₹ 270.59 lakh]</b>	<b>40.59</b>
<b>Add: Surcharge@12%</b>	<b><u>4.88</u></b>
	<b>45.47</b>
<b>Add: Education cess@2% and SHEC@1%</b>	<b><u>1.36</u></b>
<b>Dividend Distribution tax</b>	<b><u>46.83</u></b>

## **2. Accounting for DDT**

- According to generally accepted accounting principles, the provision for dividend is recognised in the financial statements of the year to which the dividend relates.
- In view of this, DDT on dividend, being directly linked to the amount of the dividend concerned, should also be reflected in the accounts of the same financial year even though the actual tax liability in respect thereof may arise in a different year.

## **3. Disclosure and Presentation of DDT in Financial Statements**

- Dividend on shares is an appropriation of profit which is not shown in the Statement of Profit and Loss as per the Schedule III to the Companies Act, 2013. It is shown

as an appropriation or allocation of profit in the 'Notes to Accounts' of the 'Reserves and Surplus' item of the Balance sheet.

- Since dividends are appropriation to profits which is not the part of disclosure in the Statement of Profit and Loss, therefore, a question arises with regard to disclosure and presentation of DDT, as to whether the said tax should also be disclosed as appropriation or should be disclosed along with the normal income-tax provision for the year.
- The liability in respect of DDT arises only if the profits are distributed as dividends whereas the normal income-tax liability arises on the earning of the taxable profits
- Since the DDT liability relates to distribution of profits as dividends which are disclosed as appropriation /allocation of profit in the 'Notes to Accounts' of 'Reserves and Surplus', it is appropriate that the liability in respect of DDT should also be disclosed therein.
- It is felt that such a disclosure would give a proper picture regarding payments involved with reference to dividends.
- DDT liability should be recognised in the accounts of the same financial year in which the dividend concerned is recognised.
- DDT liability should be disclosed separately in the 'Notes to Accounts' of 'Reserves and Surplus', as follows:

Dividend	xxxxx	
Dividend Distribution tax thereon	<u>xxxxx</u>	xxxxx

- Provision for Dividend Distribution tax should be disclosed separately under the head 'Short Term Provisions' in the balance sheet.
- The accounting treatment for Dividend Distribution tax in the financial statements of a company can be explained with the help of following example:

*X Ltd. proposed to distribute dividend amounting to ₹ 425 lacs for the year ended 31st March, 2015. The Dividend Distribution tax liability (@ 17.304%) arises as per Income-tax Act, 1961. In this case, calculate the grossing-up of dividend and separately disclosed the charge for DDT in the 'Notes to Accounts' of 'Reserves and Surplus'.*

#### **Solution**

Calculation of grossing-up of dividend:

Particulars	₹ in lacs
Dividend distributed by X CO.	425
Add: Increase for the purpose of grossing up of dividend $\left[ \frac{15}{100 - 15} \times 425 \right]$	75

## 2.28 Accounting

Gross dividend	500
Dividend distribution tax @ 17.304%	86.52

(An Extract)

- 'Notes to Accounts' of 'Reserves and Surplus'
- for the year ended 31st March, 2015

	₹ (lacs)	₹ (lacs)
Proposed Dividend	425.00	
Dividend Distribution tax	<u>86.52</u>	511.52

The provision for Dividend Distribution tax should be disclosed separately under, the head 'Short Term Provisions'. The relevant extracts of the Balance Sheet of X Ltd. can be shown as follows:

### Balance Sheet as on 31st March, 2015

	₹ (lacs)
Short term provisions	
Proposed Dividend	425.000
Dividend Distribution tax	<u>86.52</u>

### Illustration 1

The following is the Trial Balance of Omega Limited as on 31.3.2015:

(Figures in ₹'000)

	Debit		Credit
Land at cost	220	Equity Capital (Shares of ₹10 each)	300
Plant & Machinery at cost	770	10% Debentures	200
Trade Receivables	96	General Reserve	130
Inventories (31.3.15)	86	Profit & Loss A/c	72
Bank	20	Securities Premium	40
Adjusted Purchases	320	Sales	700
Factory Expenses	60	Trade Payables	52
Administration Expenses	30	Provision for Depreciation	172
Selling Expenses	30	Suspense Account	4
Debenture Interest	20		
Interim Dividend Paid	<u>18</u>		
	<u>1670</u>		<u>1670</u>

Additional Information:

- (i) The authorised share capital of the company is 40,000 shares of ₹10 each.

- (ii) The company on the advice of independent valuer wish to revalue the land at ₹ 3,60,000.
- (iii) Proposed and declared final dividend @ 10%.
- (iv) Suspense account of ₹ 4,000 represents cash received for the sale of some of the machinery on 1.4.14. The cost of the machinery was ₹ 10,000 and the accumulated depreciation thereon being ₹ 8,000.
- (v) Depreciation is to be provided on plant and machinery at 10% on cost.

You are required to prepare Omega Limited's Balance Sheet as on 31.3.2015 and Statement of Profit and Loss with notes to accounts for the year ended 31.3.2015 as per Schedule III. Ignore previous years' figures & taxation.

### Solution

#### Omega Limited Balance Sheet as at 31<sup>st</sup> March, 2015

Particulars	Note No.	(₹ in 000)
<b>Equity and Liabilities</b>		
<b>1. Shareholders' funds</b>		
a Share capital	1	300
b Reserves and Surplus	2	500
<b>2. Non-Current liabilities</b>		
a Long term borrowings	3	200
<b>3. Current liabilities</b>		
a Trade Payables		52
b Short-term provisions	4	30
<b>Total</b>		<b>1082</b>
<b>Assets</b>		
<b>1. Non-current assets</b>		
a Fixed assets		
i Tangible assets	5	880
<b>2. Current assets</b>		
a Inventories		86
b Trade receivables		96
c Cash and cash equivalents		20
<b>Total</b>		<b>1082</b>

## 2.30 Accounting

**Omega Limited**  
**Statement of Profit and Loss for the year ended 31<sup>st</sup> March, 2015**

Particulars	Notes	(₹ in 000)
I. Revenue from operations		700
II. Other Income	6	<u>2</u>
III <b>Total Revenue</b>		<b><u>702</u></b>
IV Expenses:		
Purchases		320
Finance costs	7	20
Depreciation (10% of 760)		76
Other expenses	8	<u>120</u>
<b>Total Expenses</b>		<b><u>536</u></b>
V. <b>Profit (Loss) for the period</b> (III – IV)		<b><u>166</u></b>

### Notes to accounts

			(₹ in 000)
1.	<b>Share Capital</b>		
	Equity share capital		
	Authorized		
	40,000 shares of ₹ 10 each		400
	Issued & subscribed & called up		
	30,000 shares of ₹ 10 each		300
	<b>Total</b>		<b><u>300</u></b>
2.	<b>Reserves and Surplus</b>		
	Securities Premium Account		40
	Revaluation reserve		140
	General reserve		130
	Profit & loss Balance		
	Opening balance	72	
	Profit for the period	<u>166</u>	238
	Less: Appropriations		
	Interim Dividend	(18)	
	Proposed Final Dividend	<u>(30)</u>	<u>190</u>
			<u>500</u>
3.	<b>Long term borrowing</b>		

	10% Debentures		200
4.	<b>Short term provision</b>		
	Proposed Final Dividend		30
5.	<b>Tangible assets</b>		
	<b>Land</b>		
	Opening balance	220	
	Add: Revaluation adjustment	<u>140</u>	
	Closing balance		360
	<b>Plant and Machinery</b>		
	Opening balance	770	
	Less: Disposed off	<u>(10)</u>	
		760	
	Less: Depreciation (172-8+76)	<u>(240)</u>	
	Closing balance		<u>520</u>
	<b>Total</b>		<u>880</u>
6.	<b>Other Income</b>		
	Profit on sale of machinery:		
	Sale value of machinery	4	
	Less: Book value of machinery (10-8)	<u>(2)</u>	2
7.	<b>Finance costs</b>		
	Debenture interest		20
8.	<b>Other expenses:</b>		
	Factory expenses	60	
	Selling expenses	30	
	Administrative expenses	<u>30</u>	120

**Illustration 2**

You are required to prepare Balance sheet and statement of Profit and Loss from the following trial balance of Haria Chemicals Ltd. for the year ended 31st March, 2015.

**Haria Chemicals Ltd.**  
**Trial Balance as at 31st March, 2015**

Particulars	₹	Particulars	₹
Inventory	6,80,000	Equity Shares	
Furniture	2,00,000	Capital (Shares of ₹ 10 each)	25,00,000
Discount	40,000	11% Debentures	5,00,000
Loan to Directors	80,000	Bank loans	6,45,000

## 2.32 Accounting

Advertisement	20,000	Trade payables	2,81,000
Bad debts	35,000	Sales	42,68,000
Commission	1,20,000	Rent received	46,000
Purchases	23,19,000	Transfer fees	10,000
Plant and Machinery	8,60,000	Profit & Loss account	1,39,000
Rentals	25,000	Depreciation provision:	
Current account	45,000	Machinery	1,46,000
Cash	8,000		
Interest on bank loans	1,16,000	:	
Preliminary expenses	10,000		
Fixtures	3,00,000		
Wages	9,00,000		
Consumables	84,000		
Freehold land	15,46,000		
Tools & Equipments	2,45,000		
Goodwill	2,65,000		
Trade receivables	4,40,000		
Dealer aids	21,000		
Transit insurance	30,000		
Trade expenses	72,000		
Distribution freight	54,000		
Debenture interest	<u>20,000</u>		
	<u>85,35,000</u>		<u>85,35,000</u>

Additional information : Closing Inventory on 31-3-2015: ₹ 8,23,000.

### Solution

#### Haria Chemicals Ltd.

#### Balance Sheet as at 31st March, 2015

	Schedule No. (1)	Rupees as at the end of 31st March 2015 (2)
<b>Equity and Liabilities</b>		
<b>(1) Shareholders' funds :</b>		
(a) Share Capital	1	25,00,000
(b) Reserves and Surplus	2	7,40,000



<b>(2) Non Current Liabilities</b>		
(a) Long term borrowings	3	11,45,000
<b>(3) Current Liabilities</b>		
(a) Trade payables		2,81,000
<b>Total</b>		<b>46,66,000</b>
<b>Assets</b>		
<b>(1) Non current assets</b>		
<b>Fixed Assets :</b>		
(a) Tangible assets	4	30,05,000
(b) Intangible assets(goodwill)		2,65,000
<b>(2) Current assets</b>		
(a) Inventories		8,23,000
(b) Trade receivables		4,40,000
(c) Cash and cash equivalents	5	53,000
(d) Short term loans and advances	6	80,000
<b>Total</b>		<b>46,66,000</b>

**Haria Chemicals Ltd.****Statement of Profit and Loss for the year ended 31st March, 2015**

	<i>Schedule No.</i>	<i>Figures as at the end of 31st March 2015</i>	
Revenue from operations		42,68,000	
Other income (A)	8	<u>56,000</u>	
		43,24,000	
Expenses			
Cost of materials consumed	9	23,19,000	
Change in inventory of finished goods		(1,43,000)	
Employee benefit expenses	10	9,00,000	
finance cost	11	1,36,000	
Other expenses (B)	12	<u>5,11,000</u>	
		<u>37,23,000</u>	
Profit before tax (A – B)			6,01,000
Provision for tax			<u>—</u>
Profit for the period			<u><u>6,01,000</u></u>

## 2.34 Accounting

### Notes to Accounts

<b>1. Share capital</b>			₹
Authorised :			
Equity share capital of ₹10 each			<u>25,00,000</u>
Issued and Subscribed :			
Equity share capital of ₹10 each			25,00,000
<b>2. Reserves and Surplus</b>			
Balance as per last balance sheet			1,39,000
Balance in profit and loss account			<u>6,01,000</u>
			<u>7,40,000</u>
<b>3. Long term Borrowings</b>			
11% Debentures			5,00,000
Bank loans			<u>6,45,000</u>
			<u>11,45,000</u>
<b>4. Tangible Assets</b>			
	<i>Gross block</i>	<i>Depreciation</i>	<i>Net Block</i>
Freehold land	15,46,000		15,46,000
Furniture	2,00,000		2,00,000
Fixtures	3,00,000		3,00,000
Plant & Machinery	8,60,000	1,46,000	7,14,000
Tools & Equipment	<u>2,45,000</u>		<u>2,45,000</u>
Total	31,51,000	1,46,000	30,05,000
<b>5. Cash and cash equivalents</b>			
Current account balance			45,000
Cash			<u>8,000</u>
			<u>53,000</u>
<b>6. Short-term loans and Advances</b>			
Loan to directors			80,000
<b>7. Other Income</b>			
Rent received			46,000
Transfer fees			<u>10,000</u>
			<u>56,000</u>
<b>8. Cost of materials consumed</b>			
Add: purchases			23,19,000

<b>9. Changes in inventory of finished goods, WIP &amp; Stock in trade</b>		
Opening inventory	6,80,000	
Closing inventory	<u>8,23,000</u>	(1,43,000)
<b>10. Employee benefit expense</b>		
Wages		9,00,000
<b>11. Finance cost</b>		
Interest on bank loans		1,16,000
Debenture interest		<u>20,000</u>
		<u>1,36,000</u>
<b>12. Other Expenses</b>		
Consumables		84,000
Preliminary expenses		10,000
Bad debts		35,000
Discount		40,000
Rentals		25,000
Commission		1,20,000
Advertisement		20,000
Dealers' aids		21,000
Transit insurance		30,000
Trade expenses		72,000
Distribution freight		<u>54,000</u>
		<u>5,11,000</u>

**Illustration 3**

The following are the balances from the Ledger of Mount View Hotel Ltd., on 31st March 2015:

	₹
Share Capital - Credit Balance on 1st January, 2015	56,685
Freehold Premises	46,800
Furniture and Fittings	8,934
Glass and China	1,101
Linen	840
Cutlery and Plate	390
Rates, Taxes and Insurance	1,713
Salaries	2,400
Wages	4,305
Inventories on 31st March, 2014 :	

## 2.36 Accounting

---

Wines, ₹1,239 ; Spirits, ₹378 ; Beer, ₹ 165 ;	1,782
Minerals, ₹ 147 ; Cigars and Cigarettes, ₹ 114	261
Sundry Provisions and Stores, ₹183; Coal, ₹ 150	333
Purchases :	
Meat, ₹3,627 ; Fish and Poultry ₹3,960	7,587
Sundry Provisions and Stores, ₹5,220	5,220
Wines ₹1,881 ; Spirits ₹2,190 ; Beer ₹ 1,152	5,223
Minerals, ₹1,050 : Cigars and Cigarettes, ₹240	1,290
Laundry	951
Coal and Gas	2,160
Electric Light	1,128
General Expenses	1,710
Sales —	
Wines, ₹3,870 ; Spirits, ₹4,335 ; Beer, ₹1,863	10,068
Minerals, ₹2,160 ; Cigars and Cigarettes, ₹390	2,550
Meals	23,829
Rooms	9,375
Fires in Bedrooms	582
Washing Charges	219
Repairs, Renewals, and Depreciation -	
Premises, ₹348 ; Furniture and Fittings, ₹660	1,008
Glass and China, ₹ 609 ; Linen, ₹390	999
Cutlery and Plate	207
Cash Book - Debit Balances:	
In Bank	7,500
On hand	2,367
Visitors Accounts unpaid	489
Trade payables	3,390
Inventories on 31st March, 2015 were valued as follows -	
Wines, ₹1,197; Spirits, ₹ 333 ; Beer, ₹174 ;	
Minerals, ₹357; Cigars and Cigarettes, ₹69;	
Sundry Provisions and Stores, ₹141; Coal, ₹99	

The Manager is entitled to a commission of 5% of the net profits after charging his commission. The authorised share capital is 10,000 shares of ₹10 each of which 5,700 shares were issued, the whole of the amount being called up. The final call on 210 shares @ ₹1.50 per share was unpaid; the directors forfeited these shares at their meeting held on 15th March, 2015.

The tax liability is estimated at ₹4,300 and the directors propose to declare a dividend at the rate of 6 per cent. Prepare the Balance Sheet and Statement of Profit and Loss with notes to accounts for presentation to the shareholders.

### Solution

#### Balance Sheet of Mount-View Hotel Ltd., as on 31st March, 2015

Particulars	Note No	₹
<b>Equity and Liabilities</b>		
<b>1 Shareholders' funds</b>		
a Share capital	1	56,685
b Reserves and Surplus	2	1,941.47
<b>2 Current liabilities</b>		
a Trade Payables	3	3,390
b Other current liabilities	4	510
c Short-term provisions	5	8,264.53
<b>Total</b>		<b>70,791</b>
<b>Assets</b>		
<b>1 Non-current assets</b>		
a Fixed assets		
i Tangible assets	6	55,734
<b>2 Current assets</b>		
a Inventories	7	4,701
b Trade receivables		489
c Cash and cash equivalents	8	9,867
<b>Total</b>		<b>70,791</b>

#### Statement of Profit and Loss of Mount-View Hotel Ltd., for the year ended 31st March, 2015

Particulars	Notes	₹
I. Revenue from operations (A)	9	46,623.0
II Expenses:		
Cost of materials consumed	10	7,587.0
Purchases of Inventory-in-Trade	11	11,733.0

## 2.38 Accounting

	Changes in inventories of finished goods work-in-progress and Inventory-in-Trade	12	6.0
	Employee benefits expense	13	7,215.0
	Other operating expenses	14	6,453.0
	Administrative and general expenses	15	3,423.0
	<b>Total expenses (B)</b>		<b>36,417.0</b>
III	Profit before tax (VII- VIII) (A – B)		<b>10,206.0</b>
IV	Provision for tax		(4,300.0)
V	<b>Profit (Loss) for the period</b>		<b>5,906.0</b>

### Notes to accounts

		₹
<b>1</b>	<b>Share Capital</b>	
	Equity share capital	
	Authorised	
	10,000 Shares of ₹10 each	100,000
	Issued & subscribed & called up	
	5,490 Equity Shares of ₹10 each	54,900
	Forfeited Shares (210 x 8.5)	1,785
	<b>Total</b>	<b>56,685</b>
<b>2</b>	<b>Reserves and Surplus</b>	
	Surplus (Profit & Loss A/c)	5906.0
	<b>Appropriations</b>	
	Proposed Dividend	3,294.0
	Dividend Distribution tax (W.N.)	<u>670.53</u>
	<b>Profit (Loss) carried forward to Balance Sheet</b>	<b><u>1,941.47</u></b>
<b>3</b>	<b>Trade Payables</b>	3,390
<b>4</b>	<b>Other current liabilities</b>	
	Manager's Commission Outstanding	510
<b>5</b>	<b>Short-term provisions</b>	
	Provision for taxation	4,300
	Proposed Dividend	3,294
	Dividend Distribution tax	670.53
	<b>Total</b>	<b>8,264.53</b>
<b>6</b>	<b>Tangible assets</b>	
	Freehold Premises	47,148

	Less: Depreciation	(348)	46,800
	Furniture & Fittings	9,594	
	Less: Depreciation	(660)	8,934
	<b>Total</b>		<b>55,734</b>
<b>7</b>	<b>Inventories</b>		
	Raw Material		
	Wines, Spirits & Beer	1,704	
	Minerals, Cigars & Cigarettes	426	
	Sundry Provisions & Stores and Coal	<u>240</u>	2,370
	Loose tools		
	Linen	1,230	
	Less: Depreciation	(390)	840
	Cutlery & Plate	597	
	Less: Depreciation	(207)	390
	Glass & China	1,710	
	Less: Depreciation	(609)	1,101
	<b>Total</b>		<b>4,701</b>
<b>8</b>	<b>Cash and cash equivalents</b>		
	Cash at bank		7,500
	Cash in hand		2,367
	<b>Total</b>		<b>9,867</b>
<b>9</b>	<b>Revenue from operations</b>		
	Sale of products		
	Wines, Spirits, Beer	10,068	
	Minerals, Cigars and Cigarettes	<u>2,550</u>	12,618.0
	Sale of services		
	Meals	23,829	
	Rooms	9,375	
	Fires in Bed Rooms	582	
	Washing Charges	219	34,005.0
	<b>Total</b>		<b>46,623.0</b>
<b>10</b>	<b>Cost of materials consumed</b>		
	Meat, Fish and Poultry		7,587.0
	<b>Total</b>		<b>7,587.0</b>
<b>11</b>	<b>Purchases of Inventory-in-Trade</b>		
	Wines, Spirits, Beer		5,223.0
	Minerals, Cigars & Cigarettes		1,290.0

## 2.40 Accounting

	Sundry Provisions & Stores		5,220.0
	<b>Total</b>		<b>11,733.0</b>
<b>12</b>	<b>Changes in inventories of finished goods work-in-progress and Inventory-in-Trade</b>		
	Opening Inventory		
	Wines, Spirit & Beer	1,782	
	Minerals, Cigars & Cigarettes	261	
	Sundry Provisions & Stores and Coal	333	2,376.0
	<b>Less: Closing Inventory</b>		
	Wines, Spirit & Beer	1,704	
	Minerals, Cigars & Cigarettes	426	
	Sundry Provisions & Stores and Coal	<u>240</u>	(2,370.0)
	<b>Total</b>		<b>6.0</b>
<b>13</b>	<b>Employee benefits expense</b>		
	Salaries		2,400.0
	Wages		4,305.0
	Manager's commission (on ₹10,206 @ 5%)		510.0
	<b>Total</b>		<b>7215.0</b>
<b>14</b>	<b>Other operating expenses</b>		
	Coal and Gas		2,160.0
	Laundry		951.0
	Electricity Light		1,128.0
	Repairs, Renewals and Depreciation		
	Premises	348	
	Furniture & Fittings	660	
	Glass and China	609	
	Linen	390	
	Cutlery & Plate	207	2,214.0
	<b>Total</b>		<b>6453.0</b>
<b>15</b>	<b>Administrative and general expenses</b>		
	Rates, Taxes and Insurances		1,713.0
	General Expenses		1,710.0
	<b>Total</b>		<b>3,423.0</b>



**Working Note:****Calculation of Dividend distribution tax****(i) Grossing-up of dividend:**

	₹
<b>Dividend distributed by Mount view hotel Ltd.</b>	<b>3,294</b>
<b>Add: Increase for the purpose of grossing up of dividend</b> $\left[ \frac{15}{100 - 15} \times 3,294 \right]$	<b><u>581</u></b>
<b>Gross dividend</b>	<b><u>3,875</u></b>
<b>(ii) Dividend distribution tax @ 17.304%</b>	<b>670.53</b>

**Illustration 4**

The following balances have been extracted from the books of DOW Books Limited as on 31st March, 2015.

Dr.	₹	Cr.	₹
Cash in hand	3,800	Share Capital	90,000
Cash at Bank	12,600	9% Debentures	30,000
Bills Receivable	4,000	Trade payables	29,000
Investment	1,000	Profit and Loss A/c	2,000
Security Deposit	400	Secured Loan from bank	
Advances	8,500	against stock	50,000
Trade receivables	75,000	Gross Profit	1,75,000
Land and Buildings	1,05,000	Share Suspense	3,000
Furniture	4,500	Liabilities for expenses	12,000
Motor Car	25,000	Sale of Furniture	300
Closing Inventory	95,000	Bills Payable	3,100
Establishment expenses	35,200	Miscellaneous Receipts	425
Repairs and renewals	2,600		
Motor Car Expenses	4,200		
Travelling and Conveyance	1,600		
Printing and Stationery	900		
Telephone	1,200		
Debenture Interest	2,025		
Commission on sales	3,200		
Advertisement	3,500		

## 2.42 Accounting

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Managing Director's remuneration	3,600	
Directors fees	<u>2,000</u>	
	<u>3,94,825</u>	<u>3,94,825</u>

The following further particulars are available:

- (1) Amount of share capital has been arrived at as follows -

9,200 equity shares of ₹10 each, fully called up	92,000
Less : Calls-in-arrear @ ₹ 2 on 1,000 shares	<u>(2,000)</u>
	<u>90,000</u>
- (2) The Profit and Loss Account balance has been arrived at after charging ₹5,000 on account of short provision of taxation for the earlier year.
- (3) A Bank advice, for debit of ₹710 on account of interest on loan upto 31st March 2015, was received on 5th April, 2015 the loan having been taken on 1st March, 2015.
- (4) The Bank statement shows a wrong credit of ₹3,000 on 16th March 2015, the same being detected and adjusted by the Bank on 30th April 2015.
- (5) The 1,000 shares, on which calls were forfeited by the Board, and Share Suspense represents the amount received on their reissue, as fully paid, by Board's resolution.
- (6) Sale of furniture represents disposals, during the year, of a few old items of furniture having a written-down value of ₹400 on 30th September 2014, against their original cost of ₹ 800.
- (7) Cost of land ₹30,000 is included in the amount of land and buildings.
- (8) Trade receivables, which are all unsecured and considered goods, include ₹10,000 due for more than six months.
- (9) Advertisement charges include materials of ₹ 1,500.
- (10) Advances include ₹3,000 paid for a new telephone installed during the year under the OYT Scheme, of which an amount of ₹150 has been set off against the current year's bills.
- (11) Amounts of ₹2,000 and ₹1,200 debited to purchases and wages respectively, were for making new furniture during the year.
- (12) Investment represents purchase of 200 equity shares of ₹10 each, ₹5 per share called and paid up.
- (13) Charge depreciation on the closing written down amount of -

Buildings @ 2.5%
Furniture @ 10%
Motor Car @ 20%

(14) Original costs of fixed assets were -

	₹
Buildings	1,00,000
Furniture	9,000
Motor Car	35,000

(15) The Managing Director is entitled to 5% of the annual net profits as his remuneration, subject to a minimum of ₹300 per month. The net profits, for this purpose, are to be taken without charging income-tax and his remuneration itself.

(16) Bills discounted not matured ₹1,500.

(17) Provision for income-tax is to be made, for the year, of ₹65,000.

(18) The following appropriations have been proposed by the Board of Directors out of the profit for the year -

(a) Transfer of ₹ 20,000 to General Reserve.

(b) Declared Dividend of 12% on the paid-up capital.

(19) Debentures were issued two years back, and are not secured.

You are required to prepare the Statement of Profit and Loss for the year ended 31st March, 2015 and the Balance as on that date. Ignore previous year's figures.

### Solution

#### DOW Books Ltd.

#### Statement of Profit and Loss for the year ended 31st March, 2015

Particulars	Notes	Amount
Gross profit from operations		1,75,000
Other income		425
<b>Total revenue</b>		<b>1,75,425</b>
Expenses:		
Employee benefits expense	12	7,723
Other operating expenses	13	43,600
Selling and administrative expenses	14	4,250
Finance costs	15	3,410
Depreciation and amortization expense	16	7,605
Other expenses	17	100
<b>Total expenses</b>		<b>66,688</b>
Profit before tax		<b>1,08,737</b>

## 2.44 Accounting

Provision for tax	65,000
Short Provision for Income tax in the previous year*	5,000
<b>Profit (Loss) for the period</b>	<b>38,737</b>

\*The excess tax liability is to be considered as change in accounting estimate and the effect of such change should be included in the determination of net profit or loss of the affected period, in accordance with para 23 of AS 5 (Revised).

### Note on Remuneration to Managing Director:

₹

Profit as disclosed	43,737
Add : Provision for Taxation	65,000
Managing Director's Remuneration	<u>5,723</u>
Profit before calculating the Remuneration	<u>1,14,460</u>
Remuneration @ 5%	5,723

### Balance Sheet of DOW Books Ltd., as at 31st March, 2015

Particulars	Note No	₹
<b>Equity and Liabilities</b>		
<b>1 Shareholders' funds</b>		
a Share capital	1	92,000.00
b Reserves and Surplus	2	33,450.00
<b>2 Non-current liabilities</b>		
a Long-term borrowings	3	80,000 .00
<b>3 Current liabilities</b>		
a Trade Payables	4	32,100.00
b Other current liabilities	5	15, 508.00
c Short-term provisions	6	78,287.00
<b>Total</b>		<b>3,31,345.00</b>
<b>Assets</b>		
<b>1 Non-current assets</b>		
a Fixed assets		
i Tangible assets	7	1,29,695.00
b Non-current investments	8	1,000 .00
<b>2 Current assets</b>		
a Inventories		95,000.00
b Trade receivables	9	79,000 .00

c	Cash and cash equivalents	10	16,400 .00
d	Short-term loans and advances	11	10,250.00
<b>Total</b>			<b>3,31,345.00</b>

**Note :** There is contingent liability for calls that may be made on partly paid shares, ₹1,000 and for Bills under discount, ₹ 1,500.

#### Notes to accounts

		₹
<b>1 Share Capital</b>		
Equity share capital		
Issued & subscribed & paid up		
9,200 Equity Shares of ₹ 10 each fully paid		92,000
<b>Total</b>		<b>92,000</b>
<b>2 Reserves and Surplus</b>		
Capital reserve		1,000
General reserve (proposed transfer)		20,000
Surplus (Profit & Loss A/c)	38,737	
Add: Balance from previous year	<u>7,000</u>	
	45,737	
<b>Appropriations</b>		
Proposed Dividend	(11,040 )	
Dividend Distribution tax (W.N.1)	(2,247)	
Transfer to General Reserve (proposed)	<u>(20,000)</u>	12,450
<b>Total</b>		<b>33,450</b>
<b>3 Long-term borrowings</b>		
Secured		
Loan from bank (secured against stock)		50,000
Unsecured		
9% Debentures		30,000
<b>Total</b>		<b>80,000</b>
<b>4 Trade Payables</b>		
Trade payables		29,000
Bills Payable		3,100
<b>Total</b>		<b>32,100</b>

## 2.46 Accounting

<b>5 Other current liabilities</b>		
Interest due on bank loan		710
Interest accrued on debentures		675
Liability for expenses		12,000
Managerial Remuneration (5,723 – 3,600)		2,123
<b>Total</b>		<b>15,508</b>
<b>6 Short-term provisions</b>		
Provision for taxation		65,000
Proposed Dividend		11,040
Dividend Distribution tax		2,247
<b>Total</b>		<b>78,287</b>
<b>7 Tangible assets</b>		
Land		30,000
Building	1,00,000	
Less: Depreciation	(26,875)	73,125
Furniture	9,000	
Less: Disposed off	(800)	
Add: Addition during the year	3,200	
Less: Depreciation	(4,830)	6,570
Motor Car	35,000	
Less: Depreciation	(15,000)	20,000
<b>Total</b>		<b>1,29,695</b>
<b>8 Non-current investments</b>		
Other investments		
Partly paid shares		1,000
<b>Total</b>		<b>1,000</b>
<b>9 Trade receivables</b>		
Unsecured but considered good		
More than 6 months	10,000	
Others	<u>65,000</u>	75,000
Bills Receivable		4,000
<b>Total</b>		<b>79,000</b>
<b>10 Cash and cash equivalents</b>		
Cash at bank		12,600
Cash in hand		3,800
<b>Total</b>		<b>16,400</b>

<b>11 Short-term loans and advances</b>	
Deposits	8,350
Advertisement material on hand	1,500
Security Deposit	400
<b>Total</b>	<b>10,250</b>
<b>12 Employee benefits expense</b>	
Managing Director's Remuneration	5,723
Directors' Fees	2,000
<b>Total</b>	<b>7,723</b>
<b>13 Other operating expenses</b>	
Establishment Expenses	35,200
Repairs, Renewals	2,600
Motor Car Expenses	4,200
Travelling & Conveyance	1,600
<b>Total</b>	<b>43,600</b>
<b>14 Selling and administrative expenses</b>	
Sales Commission	3,200
Advertisement	2,000
Printing & Stationery	900
Telephone	1,350
Cost of furniture (to be capitalized)	(3,200)
<b>Total</b>	<b>4,250</b>
<b>15 Finance costs</b>	
Debenture Interest	2,700
Bank Interest	710
<b>Total</b>	<b>3,410</b>
<b>16 Depreciation and amortization expense</b>	
Buildings	1,875
Furniture & Fittings	730
Motor Car	5,000
<b>Total</b>	<b>7,605</b>
<b>17 Other expenses</b>	
Loss on sale of furniture	100
<b>Total</b>	<b>100</b>

**Working Notes:****1. Calculation of Dividend distribution tax**

	₹
<b>(i) Grossing-up of dividend:</b>	<b>11,040</b>
<i>Dividend distributed by DOW Books Ltd.</i>	
<i>Add: Increase for the purpose of grossing up of dividend</i>	
$\left[ \frac{15}{100 - 15} \times 11,040 \right]$	<b><u>1,948</u></b>
<b>Gross dividend</b>	<b><u>12,988</u></b>
<b>(ii) Dividend distribution tax @ 17.304% of 12,988</b>	<b><u>2,247</u></b>

- ₹710, interest due to Bank, may also be adjusted against the bank balance, specially when the Bank is entitled to debit to company's accounts under the Loan Agreement.
- The wrong credit given by the Bank, subsequently adjusted, is only an item for the Bank Reconciliation Statement.
- The Share Suspense Account has a balance of ₹1,000 after adjustment of the amount in arrear. It has to be credited to Capital Reserve.
- ₹150 out of OYT deposit has to be treated as telephone charges.
- Previous year's figures have not been given since these are not available. Stastical information required to be disclosed under Schedule III has also not been given for the same reason.

**Illustration 5**

You are required to prepare a Statement of Profit and Loss and Balance Sheet from the following Trial Balance extracted from the books of the International Hotels Ltd., on 31st March, 2015:

	Dr. ₹	Cr. ₹
Authorised Capital-divided into 5,000 6% Preference Shares of ₹100 each and 10,000 equity Shares of ₹100 each		<u>15,00,000</u>
Subscribed Capital -		
5,000 6% Preference Shares of ₹100 each		5,00,000
Equity Capital		8,05,000
Purchases - Wines, Cigarettes, Cigars, etc.	45,800	
- Foodstuffs	36,200	
Wages and Salaries	28,300	
Rent, Rates and Taxes	8,900	



Laundry	750	
Sales - Wines, Cigarettes, Cigars, etc.		68,400
- Food		57,600
Coal and Firewood	3,290	
Carriage and Cooliage	810	
Sundry Expenses	5,840	
Advertising	8,360	
Repairs	4,250	
Rent of Rooms		48,000
Billiard		5,700
Miscellaneous Receipts		2,800
Discount received		3,300
Transfer fees		700
Freehold Land and Building	8,50,000	
Furniture and Fittings	86,300	
Inventory on hand, 1st April, 2014		
Wines, Cigarettes. Cigars, etc.	12,800	
Foodstuffs	5,260	
Cash in hand	2,200	
Cash with Bankers	76,380	
Preliminary and formation expenses	8,000	
2,000 Debentures of ₹ 100 each (6%)		2,00,000
Profit and Loss Account		41,500
Trade payables		42,000
Trade receivables	19,260	
Investments	2,72,300	
Goodwill at cost	5,00,000	
General Reserve		<u>2,00,000</u>
	<u>19,75,000</u>	<u>19,75,000</u>
Wages and Salaries Outstanding	1,280	
Inventory on 31st March, 2015		
Wines, Cigarettes and Cigars, etc.	22,500	
Foodstuffs	16,400	
Depreciation :		

## 2.50 Accounting

*Furniture and Fittings @ 5% p.a. : Land and Building @ 2% p.a.*

The Equity capital on 1st April, 2014 stood at ₹7,20,000, that is 6,000 shares fully paid and 2,000 shares ₹60 paid. The directors made a call of ₹40 per share on 1st October 2014. A shareholder could not pay the call on 100 shares and his shares were then forfeited and reissued @ ₹90 per share as fully paid. The Directors proposed to declare a dividend of 8% on equity shares, transferring any amount that may be required from General Reserve. Ignore Taxation.

### Solution

#### Statement of Profit and Loss of International Hotels Ltd. for the year ended 31st March, 2015

Particulars	Notes	Amount
I. Revenue from operations	11	1,83,200
II. Other income (Discount received)		3,300
<b>III. Total Revenue (I + II)</b>		<b>1,86,500</b>
<b>IV. Expenses:</b>		
Cost of materials consumed	12	25,060
Purchases of Inventory-in-Trade	13	45,800
Changes in inventories of finished goods work-in-progress and Inventory-in-Trade	14	(9,700)
Employee benefits expense	15	29,580
Other operating expenses	16	18,000
Selling and administrative expenses	17	14,200
Finance costs	18	12,000
Depreciation and amortization expense	19	21,315
Other expenses	10	8,000
<b>Total expenses</b>		<b>1,64,255</b>
<b>V. Profit (Loss) for the period (III - IV)</b>		<b>22,245</b>

#### Balance Sheet of International Hotels Ltd. as on 31st March, 2015

Particulars	Note No	₹
<b>Equity and Liabilities</b>		
<b>1 Shareholders' funds</b>		
a Share capital	1	13,00,000
b Reserves and Surplus	2	1,74,745

<b>2 Non-current liabilities</b>		
a Long-term borrowings	3	2,00,000
<b>3 Current liabilities</b>		
a Trade Payables	4	42,000
b Other current liabilities	5	13,280
c Short-term provisions	6	94,000
<b>Total</b>		<b>18,24,025</b>
<b>ASSETS</b>		
<b>1 Non-current assets</b>		
a Fixed assets		
i Tangible assets	7	9,14,985
ii Intangible assets (Goodwill)		5,00,000
b Non-current investments		2,72,300
<b>2 Current assets</b>		
a Inventories	8	38,900
b Trade receivables		19,260
c Cash and cash equivalents	9	78,580
<b>Total</b>		<b>18,24,025</b>

**Notes to accounts**

	₹
<b>1 Share Capital</b>	
Equity share capital	
Authorised	
10,000 Equity shares of ₹ 100 each	10,00,000
Issued & subscribed	
8,000 Equity Shares of ₹ 100 each	8,00,000
Preference share capital	
Authorised	
5,000 6% Preference shares of ₹ 100 each	5,00,000
Issued & subscribed	
5,000 6% Preference shares of ₹ 100 each	5,00,000
<b>Total</b>	<b>13,00,000</b>
<b>2 Reserves and Surplus</b>	
Capital reserve	5,000

## 2.52 Accounting

	General reserve	2,00,000	
	Less : Amount used to pay dividend	(30,255)	1,69,745
	Surplus (Profit & Loss A/c)	22,245	
	Add: Balance from previous year	41,500	
	Transfer from General Reserve	30,255	
	<b>Appropriations</b>		
	Proposed Dividend	(94,000)	-
	<b>Profit (Loss) carried forward to Balance Sheet</b>	<b>0</b>	<b>0</b>
	<b>Total</b>		<b><u>1,74,745</u></b>
<b>3</b>	<b>Long-term borrowings</b>		
	Secured		
	6% Debentures		2,00,000
	<b>Total</b>		<b><u>2,00,000</u></b>
<b>4</b>	<b>Trade Payables</b>		42,000
<b>5</b>	<b>Other current liabilities</b>		
	Wages and Salaries Outstanding	1,280	
	Interest on debentures	<u>12,000</u>	13,280
<b>6</b>	<b>Short-term provisions</b>		
	Proposed dividend		
	Preference Dividend		30,000
	Equity Dividend		64,000
	<b>Total</b>		<b><u>94,000</u></b>
<b>7</b>	<b>Tangible assets</b>		
	Freehold land & Buildings	8,50,000	
	Less: Depreciation	(17,000)	8,33,000
	Furniture and Fittings	86,300	
	Less: Depreciation	(4,315)	81,985
	<b>Total</b>		<b><u>9,14,985</u></b>
<b>8</b>	<b>Inventories</b>		
	Wines, Cigarettes & Cigars, etc.		22,500
	Foodstuffs		<u>16,400</u>
	<b>Total</b>		<b><u>38,900</u></b>
<b>9</b>	<b>Cash and cash equivalents</b>		
	Cash at bank		76,380
	Cash in hand		<u>2,200</u>
	<b>Total</b>		<b><u>78,580</u></b>

<b>10</b>	<b>Other expenses</b>		
	Preliminary Expenses*		<u>8,000</u>
	<b>Total</b>		<b><u>8,000</u></b>
<b>11</b>	<b>Revenue from operations</b>		
	Sale of products		
	Wines, Cigarettes, Cigars etc.	68,400	
	Food	57,600	1,26,000
	<b>Sale of services</b>		
	Room Rent	48,000	
	Billiards	5,700	
	Miscellaneous Receipts	2,800	
	Transfer fees	700	57,200
	<b>Total</b>		<b><u>1,83,200</u></b>
<b>12</b>	<b>Cost of materials consumed</b>		
	Opening Inventory	5,260	
	Add: Purchases during the year	36,200	
	Less: Closing Inventory	(16,400)	25,060
	<b>Total</b>		<b><u>25,060</u></b>
<b>13</b>	<b>Purchases of Inventory-in-Trade</b>		
	Wines, Cigarettes etc.		45,800
	<b>Total</b>		<b><u>45,800</u></b>
<b>14</b>	<b>Changes in inventories of finished goods work-in-progress and Inventory-in-Trade</b>		
	Wines, Cigarettes etc.		
	Opening Inventory	12,800	
	Less: Closing Inventory	(22,500)	(9,700)
	<b>Total</b>		<b><u>(9,700)</u></b>
<b>15</b>	<b>Employee benefits expense</b>		
	Wages and Salaries	28,300	
	Add: Wages and Salaries Outstanding	1,280	29,580
	<b>Total</b>		<b><u>29,580</u></b>
<b>16</b>	<b>Other operating expenses</b>		
	Rent, Rates and Taxes		8,900
	Coal and Firewood		3,290
	Laundry		750

\* As per para 56 of AS 26, preliminary expenses are not shown in the balance sheet.

## 2.54 Accounting

	Carriage and Cooliage		810
	Repairs		4,250
	<b>Total</b>		<b>18,000</b>
<b>17</b>	<b>Selling and administrative expenses</b>		
	Advertising		8,360
	Sundry Expenses		5,840
	<b>Total</b>		<b>14,200</b>
<b>18</b>	<b>Finance costs</b>		
	Interest on Debentures		12,000
	<b>Total</b>		<b>12,000</b>
<b>19</b>	<b>Depreciation and amortization expense</b>		
	Land and Buildings	17,000	
	Furniture & Fittings	4,315	21,315
	<b>Total</b>		<b>21,315</b>

### Illustration 6

From the following particulars furnished by Pioneer Ltd., prepare the Balance Sheet as at 31st March, 2015 as required by Schedule III of the Companies Act. Give notes at the foot of the Balance Sheet as may be found necessary -

	Debit ₹	Credit ₹
Equity Capital (Face value of ₹100)		10,00,000
Calls in Arrears	1,000	
Land	2,00,000	
Building	3,50,000	
Plant and Machinery	5,25,000	
Furniture	50,000	
General Reserve		2,10,000
Loan from State Financial Corporation		1,50,000
Inventory :		
Finished Goods	2,00,000	
Raw Materials	<u>50,000</u>	
Provision for Taxation		68,000
Trade receivables	2,00,000	
Advances	42,700	
Proposed Dividend		60,000
Profit and Loss Account		86,700

Cash Balance	30,000	
Cash at Bank	2,47,000	
Loans (Unsecured)		1,21,000
Trade payables (For Goods and Expenses)		<u>2,00,000</u>
	<u>18,95,700</u>	<u>18,95,700</u>

The following additional information is also provided :

- (1) 2,000 equity shares were issued for consideration other than cash.
- (2) Trade receivables of ₹52,000 are due for more than six months.
- (3) The cost of assets:
 

Building	₹ 4,00,000
Plant and Machinery	₹ 7,00,000
Furniture	₹ 62,500
- (4) The balance of ₹ 1,50,000 in the loan account with State Finance Corporation is inclusive of ₹7,500 for interest accrued but not due. The loan is secured by hypothecation of the Plant and Machinery.
- (5) Balance at Bank includes ₹2,000 with Perfect Bank Ltd., which is not a Scheduled Bank.
- (6) The company had contract for the erection of machinery at ₹1,50,000 which is still incomplete.

### Solution

#### Pioneer Ltd. Balance Sheet as on 31st March, 2015

Particulars	Notes	₹
<b>Equity and Liabilities</b>		
<b>1 Shareholders' funds</b>		
a Share capital	1	9,99,000
b Reserves and Surplus	2	2,96,700
<b>2 Non-current liabilities</b>		
a Long-term borrowings	3	2,63,500
<b>3 Current liabilities</b>		
a Trade Payables		2,00,000
b Other current liabilities	4	7,500
c Short-term provisions	5	1,28,000
<b>Total</b>		<b>18,94,700</b>

## 2.56 Accounting

<b>Assets</b>		
<b>1 Non-current assets</b>		
a Fixed assets		
Tangible assets	6	11,25,000
<b>2 Current assets</b>		
a Inventories	7	2,50,000
b Trade receivables	8	2,00,000
c Cash and cash equivalents	9	2,77,000
d Short-term loans and advances		42,700
<b>Total</b>		<b>18,94,700</b>

### Notes to accounts

			₹.
<b>1 Share Capital</b>			
Equity share capital			
Issued & subscribed & called up			
10,000 Equity Shares of ₹100 each	10,00,000		
(Of the above 2,000 shares have been issued for consideration other than cash)			
Less: Calls in arrears	(1,000)		9,99,000
<b>Total</b>			<b>9,99,000</b>
<b>2 Reserves and Surplus</b>			
General Reserve			2,10,000
Surplus (Profit & Loss A/c)			86,700
<b>Total</b>			<b>2,96,700</b>
<b>3 Long-term borrowings</b>			
Secured			
Term Loans			
Financial Corporation			1,42,500
(Secured by hypothecation of Plant and Machinery)			
Unsecured			1,21,000
<b>Total</b>			<b>2,63,500</b>
<b>4 Other current liabilities</b>			
Interest accrued but not due on loans (SFC)			7,500
<b>Total</b>			<b>7,500</b>



<b>5 Short-term provisions</b>		
Provision for taxation		68,000
Proposed Dividend		60,000
<b>Total</b>		<b>1,28,000</b>
<b>6 Tangible assets</b>		
Land		2,00,000
Buildings	4,00,000	
Less: Depreciation	(50,000)	3,50,000
Plant & Machinery	7,00,000	
Less: Depreciation	(1,75,000)	5,25,000
Furniture & Fittings	62,500	
Less: Depreciation	(12,500)	50,000
<b>Total</b>		<b>11,25,000</b>
<b>7 Inventories</b>		
Raw Material		50,000
Finished goods		2,00,000
<b>Total</b>		<b>2,50,000</b>
<b>8 Trade receivables</b>		
Debts outstanding for a period exceeding six months		52,000
Other Debts		1,48,000
<b>Total</b>		<b>2,00,000</b>
<b>9 Cash and cash equivalents</b>		
Cash at bank		
with Scheduled Banks	2,45,000	
with others (Perfect Bank Ltd.)	2,000	2,47,000
Cash in hand		30,000
<b>Total</b>		<b>2,77,000</b>

**Notes:** Estimated amount of contract remaining to be executed on capital account and not provided for ₹1,50,000.\*

\* It has been assumed that the company had given this contract for purchase of machinery.

## Summary

1. Meaning of Company has been defined Companies Act, 2013.
2. Books of accounts should be maintained at Registered office of company. Proper books are not deemed to be kept if they do not provide a true and fair view of state of affairs of company.

## **2.58     Accounting**

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3. A number of Statutory Books have been prescribed under Companies Act which is to be maintained along with statistical books to keep a record of all transactions.
4. Annual Return is to be filed by every company within 60 days of holding Annual general meeting.
5. Financial statements of a company should be as per schedule III and they should give true and fair view.
6. Managerial Remuneration calculated as a percentage on profit and is governed by various sections of the Companies Act, 2013.
7. Following things have been dealt with under various sections :
  - (a) Overall maximum managerial remuneration payable
  - (b) Managerial remuneration in case of absence or inadequacy of profits
  - (c) Remuneration payable to whole-time directors and part-time directors
  - (d) Ascertaining net profit of company
  - (e) Remuneration of manager
8. Determining amount of profits available for distribution is an important function and depends on a number of factors, like their composition, the amount of provisions and appropriations that must be made out of them in priority, etc.
9. Capital cannot be returned to shareholders by way of dividend.
10. Appropriating a part of profits may be done as a result of decision of Board of directors or as per law.
11. Dividend may be declared out of reserves subject to certain conditions. Dividends cannot be declared except out of profits
12. Capital reserves include reserves which are not intended for distribution and include profit prior to incorporation, on sale of fixed assets profit on reissue of forfeited shares, credit balance in capital reduction account. In short only profits or a surplus of a capital nature can be credited to such a reserve.
13. Holders of preference shares are entitled to receive a dividend at a fixed rate before any dividend is declared on equity shares.
14. Dividend Distribution Tax is the amount charged on amount declared as dividend distributed or paid by such company by way of dividends (whether interim or otherwise). It shall be treated as the final payment of tax on the dividends and no further credit therefore shall be claimed by the company or by any person in respect of the tax so paid.

## Unit – 2 : Cash Flow Statement

### Learning Objectives

After studying this unit, you will be able to:

- ◆ Define cash flow statement as per AS 3
- ◆ Differentiate operating, investing and financing activities
- ◆ Learn the various elements of cash and cash equivalents
- ◆ Prepare cash flow statement both by direct method and indirect method.

### 2.1 Introduction

Accounting Standard 3, Cash Flow Statements, was issued in March, 2004. It is based on cash concept of profit. Cash Flow refers both cash and cash equivalents. This statement provides relevant information in assessing a company's liquidity, quality of earnings and solvency.

#### Benefits:

- (a) Cash flow statement provides information about the changes in cash and cash equivalents of an enterprise.
- (b) Identifies cash generated from trading operations.
- (c) The operating cash surplus which can be applied for investment in fixed assets.
- (d) Portion of cash from operations is used to pay dividend and tax and the other portion is ploughed back.
- (e) Very useful tool of planning.

#### Purpose:

Cash flow statements are prepared to explain the cash movements between two points of time.

#### Sources of Cash:

1. Issue of shares and debentures and raising long-term loan.
2. Sale of investments and other fixed assets.
3. Cash from operations (Net Operating Profit)
4. Decrease in Cash.

#### Applications of Cash

1. Redemption of preference shares and debentures and repayment of long-term loan.
2. Purchase of investments and other fixed assets.
3. Payment of tax.

## 2.60 Accounting

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4. Payment of dividend.
5. Increase in cash.
6. Loss on Operation (Net Operating Loss)

Note – Cash includes Bank A/c also. Increase in cash or decrease in cash is put in the applications and the sources respectively just to balance the cash flow statement.

At this juncture students may note that in cash flow statement changes in all balance sheet items are to be taken into consideration separately for explaining movement of cash.

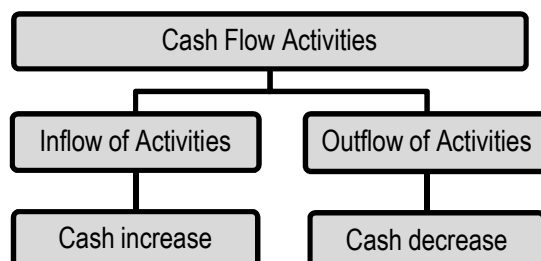
### 2.2 Elements of Cash

As per AS 3, issued by the Council of the ICAI, 'Cash' include:

- (i) Cash in hand,
- (ii) Demand deposits with banks, and
- (iii) Cash equivalents.
  - (a) Components
    - Short term highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value
    - Securities with short maturity period of, say, three months or less from the date of acquisition
  - (b) Objective
    - Deploy, for a short period, idle cash required to meet short-term cash-commitments.
  - (c) Examples
    - Acquisition of preference shares, shortly before their specified redemption date, bank deposits with short maturity period, etc.

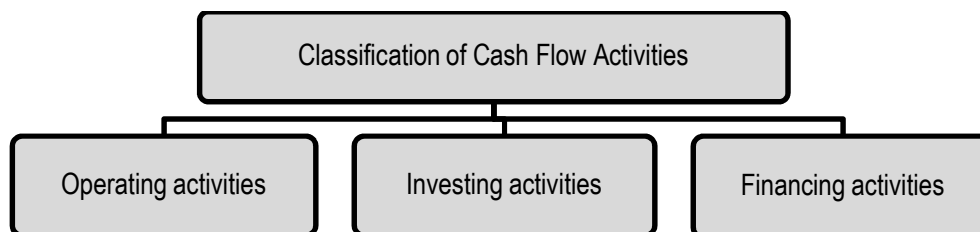
**Conclusion:** Thus, cash flow statement deals with flow of cash funds but does not consider the movements among cash, bank balance payable on demand and investment of excess cash in cash equivalents. Examples are cash withdrawn from current account, cash deposited in bank for 60 days, etc.

## 2.3 Classification of Cash Flow Activities



AS 3 provides explanation for changes in cash position of the business entity.

As per Accounting Standard 3, cash flows during the period are classified as



### 2.3.1 Operating Activities

1. *Definition:* These are the principal revenue generating activities of the enterprise.
2. *Net Impact:* Net impact of operating activities on flow of cash is reported as 'Cash flows from operating activities' or 'cash from operation'.
3. *Key Indicator:* The amount of cash flows from operating activities is a key indicator of the extent to which the operations of the enterprises have generated sufficient cash flows to :
  - (a) Maintain the operating capability of the enterprise,
  - (b) Pay dividends, repay loans, and
  - (c) Make new investments without recourse to external sources of financing.
4. *Information Provided:* It provides useful information about internal financing.
5. *Benefits:* Information about the specific components of historical operating cash flows is useful, in conjunction with other information, in forecasting future operating cash flows.

### 2.3.2 Investing activities

1. *Definition:* These are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

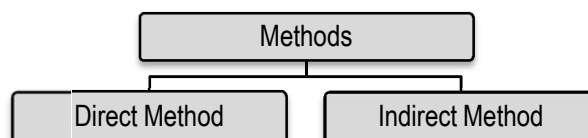
2. *Separate Disclosure*: Separate disclosure of cash flows arising from investing activities is important because the cash flows represent the extent to which the expenditures have been made for resources intended to generate future incomes and cash flows.

### 2.3.3 Financing activities

1. *Definition*: These are the activities that result in changes in the size and composition of the owner's capital (including preference share capital) and borrowings of the enterprise.
2. *Separate Disclosure*: The separate disclosure of cash flows arising from financing activities is important because it is useful in predicting claims on future cash flows by providers of funds (both capital and borrowings) to the enterprise.

## 2.4 Calculation of Cash Flows from Operating Activities

1. *Components*: Cash flows from operating activities result from the transactions and other events that enter into the determination of net profit or loss.
2. *Examples*
  - (a) cash receipts from the sale of goods and the rendering of services;
  - (b) cash receipt from fees, commission and other revenue;
  - (c) cash payments to suppliers for goods; cash payments to employees and so on.
3. *Methods*: An enterprise can determine cash flows from operating activities using either:



(a) **Direct Method**: The direct method, whereby major classes of gross cash receipts and gross cash payments are considered; or

(b) **Indirect Method**: The indirect method, whereby net profit or loss is adjusted for the effects of transactions of a non-cash nature, deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing activities.

### 2.4.1 Direct Method

1. *Information Required*
  - (a) Gross receipts and gross cash payments may be obtained from the accounting records to ascertain cash flows from operating activities.
  - (b) For example,
    - (i) information about cash received from trade receivables,

- (ii) payment to trade payables, cash expenses etc., which may be obtained by an analysis of cash book.
- (c) In actual practice, the relevant information is obtained by adjusting sales, cost of sales and other items in the profit and loss accounts for:
  - Changes during the period in inventories and operating receivables and payables;
  - Other non-cash items such as depreciation on fixed assets, goodwill written off, preliminary expenses written off, loss or gain on sale of fixed assets etc.; and
  - Other items for which the cash effects are investing or financing cash flows. Examples are interest received and paid, dividend received and paid etc., which are related to financing or investing activities and are shown separately in the cash flow statement.
  - This procedure of computation of cash flows from operating activities is also known as income statement method.
- 2. The direct method provides information which may be useful in estimating future cash flows and which is not available under the indirect method and is, therefore, considered more appropriate than the indirect method.
- 3. However, indirect method of determining the cash from operating activities is more popular in actual practice.

### 2.4.2 Indirect Method

#### Method of Determination

Under the indirect method, the net cash from operating activities is determined by adjusting net profit or loss instead of individual items appearing in the profit and loss account. Net profit or loss is also adjusted for the effect of:

- (a) changes during the period in inventories and operating receivables and payables;
- (b) non-cash items such as depreciation; and
- (c) all other items for which the cash effects are financing or investing cash flows.
- (d) The indirect method is also known as 'reconciliation method'.

### 2.4.3 Conclusion

1. It is worth noting that both direct and indirect methods adjust current assets and current liabilities related to operating activities to determine cash from operating activities.
2. But direct method adjust individual items of profit and loss account and indirect method adjusts overall net profit (or loss) to determine cash from operation.

## 2.64 Accounting

3. Therefore, indirect method fails to provide break-up of cash from operations.

### Proforma of 'Cash Flow from Operating Activities' by indirect method

		₹
Net Profit for the year		-
Add: Non-Cash and Non-Operating Expenses:	-	
Depreciation	-	
Share Discount Written off	-	
Loss on Sale of Assets	-	
Provision for taxation, etc.	-	
Less: Non-Cash and Non-Operating Incomes:		
Profit on Sale of Assets	-	
Net Profit after Adjustment for Non-Cash Items		(-)
Cash from operation	=	Net Profit (after adjustment for Non-cash Items)
	-	Increase in Current Assets
	+	Decrease in Current Asset
	+	Increase in Current Liabilities
	-	Decrease in Current Liability

## 2.5 Calculation of Cash Flows from Investing Activities

1. These activities are related to the acquisition and disposal of long-term assets, non-operating current assets and investments which results in outflow of cash.
2. Disposal of the aforesaid assets results in inflow of cash.
3. Thus, inflows and outflows related to acquisition and disposal of assets, other than those related to operating activities, are shown under this category

## 2.6 Calculation of Cash Flows from Financing Activities

1. These activities are basically related to the changes in capital and borrowing of the enterprise which affect flow of cash.
2. Redemption of shares and repayment of borrowings results in outflow of cash.
3. Thus inflows and outflows related to the amount of capital and borrowings of the enterprise are shown under this head.

Students are advised to refer full text of revised Accounting Standard on Cash Flow Statements (AS 3) for the better understanding of the chapter.



## 2.7 Illustrations

### Illustration 1

Following are the extracts of Balance Sheet of Ajay Ltd.:

Liabilities	31.3.2014	31.3.2015	Assets	31.3.2014	31.3.2015
	₹	₹			₹
Share Capital	5,00,000	5,00,000	Discount on		
15% Debentures	5,00,000	7,50,000	issue of shares	1,15,000	90,000
Unpaid Interest	--	5,000	Discount on issue		
Profit & Loss A/c	50,000	90,000	of Debentures	90,000	1,15,000

You are required to show the related items in Cash Flow Statement, if Discount on issue of Debentures amounting to ₹10,000 has been written off during the year.

### Solution

#### An Extract of Cash Flow Statement for the year ending 31.3.2015

	₹
Closing balance as per Profit & Loss A/c	90,000
Less: Opening balance as per Profit & Loss Alc.	(50,000)
Add: Discount on issue of Shares	25,000
Add: Discount on issue of Debentures	10,000
Interest on Debentures	75,000
Net Cash from Operating Activities	1,50,000

#### Cash flows from financing activities:

Proceeds from debentures	2,15,000
Interest paid on Debentures [less unpaid]	(70,000)
Net Cash from Financing Activities	1,45,000

### Working Note:

#### (i) Discount on issue of Debentures Account

Particulars	₹	Particular	₹
To Balance b/d	90,000	By Profit & Loss A/c (w/o)	10,000
To 15% Debentures A/c (Bal. fig.)	35,000	By Balance c/d	1,15,000
	1,25,000		1,25,000

## 2.66 Accounting

### (ii) 15% Debentures Account

Particulars	₹	Particular	₹
To Balance c/d	7,50,000	By Balance b/d	5,00,000
		By Bank A/c (Bal. fig.)	2,15,000
		By Discount on issue of Debentures A/c	35,000
	7,50,000		7,50,000

### Illustration 2

From the following information, calculate cash flow from operating activities:

#### Summary of Cash Account for the year ended March 31, 2015

Particulars	₹	Particulars	₹
To Balance b/d	1,00,000	By Cash Purchases	1,20,000
To Cash sales	1,40,000	By Trade payables	1,57,000
To Trade receivables	1,75,000	By Office & Selling Expenses	75,000
To Trade Commission	50,000	By Income Tax	30,000
To Sale of Investment	30,000	By Investment	25,000
To Loan from Bank	1,00,000	By Repay of Loan	75,000
To Interest & Dividend	1,000	By Interest on loan	10,000
		By Balance c/d	1,04,000
	5,96,000		5,96,000

### Solution

#### Cash Flow Statement of ..... for the year ended March 31, 2015 (Direct Method)

Particulars	₹	₹
<b>Operating Activities:</b>		
Cash received from sale of goods	1,40,000	
Cash received from Trade receivables	1,75,000	
Trade Commission received	50,000	3,65,000
Less: Payment for Cash Purchases	1,20,000	
Payment to Trade payables	1,57,000	
Office and Selling Expenses	75,000	
Payment for Income Tax	30,000	(3,82,000)
Net Cash Flow used in Operating Activities		(17,000)

**Illustration 3**

The following summary cash account has been extracted from the company's accounting records:

**Summary Cash Account**

		(₹ '000)
Balance at 1.3.2014		35
Receipts from customers		2,783
Issue of shares		300
Sale of fixed assets		<u>128</u>
		3,246
Payments to suppliers	2,047	
Payments for fixed assets	230	
Payments for overheads	115	
Wages and salaries	69	
Taxation	243	
Dividends	80	
Repayments of bank loan	<u>250</u>	<u>(3,034)</u>
Balance at 31.12.2014		<u>212</u>

Prepare Cash Flow Statement of this company Hills Ltd. for the year ended 31st March, 2015 in accordance with AS-3 (Revised).

The company does not have any cash equivalents.

**Solution**

**Hills Ltd.**  
**Cash Flow Statement for the year ended 31st March, 2015**  
**(Using direct method)**

		(₹ '000)
<b>Cash flows from operating activities</b>		
Cash receipts from customers	2,783	
Cash payments to suppliers	(2,047)	
Cash paid to employees	(69)	
Other cash payments (for overheads)	<u>(115)</u>	
Cash generated from operations	552	
Income taxes paid	<u>(243)</u>	
Net cash from operating activities		309
<b>Cash flows from investing activities</b>		
Payments for purchase of fixed assets	(230)	
Proceeds from sale of fixed assets	<u>128</u>	

## 2.68 Accounting

<i>Net cash used in investing activities</i>		(102)
<b>Cash flows from financing activities</b>		
Proceeds from issuance of share capital	300	
Bank loan repaid	(250)	
Dividend paid	<u>(80)</u>	
<i>Net cash used in financing activities</i>		<u>(30)</u>
<b>Net increase in cash and cash equivalents</b>		177
<b>Cash and cash equivalents at beginning of period</b>		<u>35</u>
<b>Cash and cash equivalents at end of period</b>		<u>212</u>

### Illustration 4

The following data were provided by the accounting records of Ryan Ltd. at year-end, March 31, 2015:

#### Income Statement

		₹
Sales		6,98,000
Cost of Goods Sold		<u>(5,20,000)</u>
Gross Margin		1,78,000
Operating Expenses		
(including Depreciation Expense of ₹ 37,000)		<u>(1,47,000)</u>
		31,000
Other Income / (Expenses)		
Interest Expense paid	(23,000)	
Interest Income received	6,000	
Gain on Sale of Investments	12,000	
Loss on Sale of Plant	<u>(3,000)</u>	
		<u>(8,000)</u>
		23,000
Income tax		<u>(7,000)</u>
		<u>16,000</u>

#### Comparative Balance Sheets

	31st March 2015	31st March 2014
<b>Assets</b>		
Plant Assets	7,15,000	5,05,000
Less: Accumulated Depreciation	<u>(1,03,000)</u>	<u>(68,000)</u>

	6,12,000	4,37,000
Investments (Long term)	1,15,000	1,27,000
Current Assets:		
Inventory	1,44,000	1,10,000
Accounts receivable	47,000	55,000
Cash	46,000	15,000
Prepaid expenses	<u>1,000</u>	<u>5,000</u>
	<u>9,65,000</u>	<u>7,49,000</u>
<b>Liabilities</b>		
Share Capital	4,65,000	3,15,000
Reserves and surplus	1,40,000	1,32,000
Bonds	2,95,000	2,45,000
Current liabilities:		
Accounts payable	50,000	43,000
Accrued liabilities	12,000	9,000
Income taxes payable	<u>3,000</u>	<u>5,000</u>
	<u>9,65,000</u>	<u>7,49,000</u>

**Analysis of selected accounts and transactions during 2014-15**

1. Purchased investments for ₹ 78,000.
2. Sold investments for ₹ 1,02,000. These investments cost ₹ 90,000.
3. Purchased plant assets for ₹ 1,20,000.
4. Sold plant assets that cost ₹ 10,000 with accumulated depreciation of ₹ 2,000 for ₹ 5,000.
5. Issued ₹ 1,00,000 of bonds at face value in an exchange for plant assets on 31st March, 2015.
6. Repaid ₹ 50,000 of bonds at face value at maturity.
7. Issued 15,000 shares of ₹ 10 each.
8. Paid cash dividends ₹ 8,000.

Prepare Cash Flow Statement as per AS-3 (Revised), using indirect method.

## 2.70 Accounting

### Solution

**Ryan Ltd.**  
**Cash Flow Statement**  
**for the year ending 31st March, 2015**

	₹	₹
<b>Cash flows from operating activities</b>		
Net profit before taxation	23,000	
Adjustments for:		
Depreciation	37,000	
Gain on sale of investments	(12,000)	
Loss on sale of plant assets	3,000	
Interest expense	23,000	
Interest income	<u>(6,000)</u>	
Operating profit before working capital changes	68,000	
Decrease in accounts receivable	8,000	
Increase in inventory	(34,000)	
Decrease in prepaid expenses	4,000	
Increase in accounts payable	7,000	
Increase in accrued liabilities	<u>3,000</u>	
Cash generated from operations	56,000	
Income taxes paid*	<u>(9,000)</u>	
<i>Net cash generated from operating activities</i>		47,000
<b>Cash flows from investing activities</b>		
Purchase of plant assets	(1,20,000)	
Sale of plant assets	5,000	
Purchase of investments	(78,000)	
Sale of investments	1,02,000	
Interest received	<u>6,000</u>	
<i>Net cash used in investing activities</i>		(85,000)
<b>Cash flows from financing activities</b>		
Proceeds from issuance of share capital	1,50,000	
Repayment of bonds	(50,000)	
Interest paid	(23,000)	
Dividends paid	<u>(8,000)</u>	
<i>Net cash from financing activities</i>		<u>69,000</u>
<b>Net increase in cash and cash equivalents</b>		31,000
<b>Cash and cash equivalents at the beginning of the period</b>		<u>15,000</u>
<b>Cash and cash equivalents at the end of the period</b>		<u>46,000</u>

**\*Working Note:**

	₹
Income taxes paid:	
Income tax expense for the year	7,000
Add: Income tax liability at the beginning of the year	<u>5,000</u>
	12,000
Less: Income tax liability at the end of the year	<u>(3,000)</u>
	<u>9,000</u>

**Illustration 5**

The balance sheets of Sun Ltd. for the years ended 31st March 2015 and 2014 were summarised as:

	2015 ₹	2014 ₹
Equity Share Capital	60,000	50,000
Reserves:		
Profit and Loss Account	5,000	4,000
Current Liabilities:		
Trade payables	4,000	2,500
Taxation	1,500	1,000
Proposed dividends	<u>2,000</u>	<u>1,000</u>
	<u>72,500</u>	<u>58,500</u>
Fixed Assets (at w.d.v.)		
Premises	10,000	10,000
Fixtures	17,000	11,000
Vehicles	12,500	8,000
Short-term investments	2,000	1,000
Current Assets		
Inventory	17,000	14,000
Trade receivables	8,000	6,000
Bank and Cash	<u>6,000</u>	<u>8,500</u>
	<u>72,500</u>	<u>58,500</u>

The profit and loss account for the year ended 31st March, 2015 disclosed

	₹
Profit before tax	4,500
Taxation	<u>(1,500)</u>
Profit after tax	3,000
Proposed dividends	<u>(2,000)</u>
Retained profit	<u>1,000</u>

## 2.72 Accounting

### Further information is available

	Fixtures ₹	Vehicles ₹
Depreciation for year	<u>1,000</u>	<u>2,500</u>
Disposals:		
Proceeds on disposal	—	1,700
Written down value	—	<u>(1,000)</u>
Profit on disposal		<u>700</u>

Prepare a Cash Flow Statement for the year ended 31st March, 2015.

### Solution

#### Sun Ltd. Cash Flow Statement for the year ended 31st March, 2015

	₹	₹
<b>Cash flows from operating activities</b>		
Net Profit before taxation	4,500	
Adjustments for:		
Depreciation	3,500	
Profit on sale of vehicles	<u>(700)</u>	
Operating profit before working capital changes	7,300	
Increase in Trade receivables	(2,000)	
Increase in inventories	(3,000)	
Increase in Trade payables	<u>1,500</u>	
Cash generated from operations	3,800	
Income taxes paid	<u>(1,000)</u>	
Net cash generated from operating activities		2,800
<b>Cash flows from investing activities</b>		
Sale of vehicles	1,700	
Purchase of vehicles	(8,000)	
Purchase of fixtures	<u>(7,000)</u>	
Net cash used in investing activities		(13,300)
<b>Cash flows from financing activities</b>		
Issue of shares for cash	10,000	
Dividends paid	<u>(1,000)</u>	
Net cash from financing activities		<u>9,000</u>
<b>Net decrease in cash and cash equivalents</b>		(1,500)
<b>Cash and cash equivalents at beginning of period (See Note 1)</b>		<u>9,500</u>
<b>Cash and cash equivalents at end of period (See Note 1)</b>		<u>8,000</u>



**Note to the Cash Flow Statement****Cash and Cash Equivalents**

	31.3.2015	31.3.2014
Bank and Cash	6,000	8,500
Short-term investments	<u>2,000</u>	<u>1,000</u>
Cash and cash equivalents	<u>8,000</u>	<u>9,500</u>

**Working Notes:**

	₹	
1. Income taxes paid		
Income tax expense for the year		1,500
Add: Income tax liability at the beginning of the year		<u>1,000</u>
		2,500
Less: Income tax liability at the end of the year		<u>(1,500)</u>
		<u>1,000</u>
2. Dividend paid		
Proposed dividend for the year		2,000
Add: Amount payable at the beginning of the year		<u>1,000</u>
		3,000
Less: Amount payable at the end of the year		<u>(2,000)</u>
		<u>1,000</u>
3. Fixed assets acquisitions		
	<i>Fixtures</i>	<i>Vehicles</i>
	₹	₹
W.D.V. at 31.3.2015	17,000	12,500
Add back:		
Depreciation for the year	1,000	2,500
Disposals	<u>—</u>	<u>1,000</u>
	18,000	16,000
Less: W.D.V. at 31.12.2014	<u>(11,000)</u>	<u>(8,000)</u>
Acquisitions during 2014-2015	<u>7,000</u>	<u>8,000</u>

**Illustration 6**

Ms. Jyoti of Star Oils Limited has collected the following information for the preparation of cash flow statement for the year ended 31<sup>st</sup> March, 2015 :

## 2.74 Accounting

	(₹ in lakhs)
Net Profit	25,000
Dividend (including dividend tax) paid	8,535
Provision for Income tax	5,000
Income tax paid during the year	4,248
Loss on sale of assets (net)	40
Book value of the assets sold	185
Depreciation charged to Profit & Loss Account	20,000
Profit on sale of Investments	100
Carrying amount of Investment sold	27,765
Interest income on investments	2,506
Interest expenses of the year	10,000
Interest paid during the year	10,520
Increase in Working Capital (excluding Cash & Bank Balance)	56,081
Purchase of fixed assets	14,560
Investment in joint venture	3,850
Expenditure on construction work in progress	34,740
Proceeds from calls in arrear	2
Receipt of grant for capital projects	12
Proceeds from long-term borrowings	25,980
Proceeds from short-term borrowings	20,575
Opening cash and Bank balance	5,003
Closing cash and Bank balance	6,988

Prepare the Cash Flow Statement for the year 2015 in accordance with AS 3. (Make necessary assumptions).

**Solution**

**Star Oils Limited**  
**Cash Flow Statement**  
**for the year ended 31st March, 2015**

(₹ in lakhs)

**Cash flows from operating activities**

Net profit before taxation (25,000 + 5,000)	30,000	
Adjustments for :		
Depreciation	20,000	
Loss on sale of assets (Net)	40	
Profit on sale of investments	(100)	
Interest income on investments	(2,506)	
Interest expenses	10,000	
Operating profit before working capital changes	57,434	
Changes in working capital (Excluding cash and bank balance)	(56,081)	
Cash generated from operations	1,353	
Income taxes paid	(4,248)	
Net cash used in operating activities		(2,895)

**Cash flows from investing activities**

Sale of assets	145	
Sale of investments (27,765 + 100)	27,865	
Interest income on investments	2,506	
Purchase of fixed assets	(14,560)	
Investment in joint venture	(3,850)	
Expenditure on construction work-in progress	(34,740)	
Net cash used in investing activities		(22,634)

**Cash flows from financing activities**

Proceeds from calls in arrear	2	
Receipts of grant for capital projects	12	
Proceeds from long-term borrowings	25,980	
Proceed from short-term borrowings	20,575	
Interest paid	(10,520)	
Dividend (including dividend tax) paid	(8,535)	27,514
Net increase in cash and cash equivalents		1,985
Cash and cash equivalents at the beginning of the period		5,003
Cash and cash equivalents at the end of the period		<u>6,988</u>

## 2.76 Accounting

### Working note :

Book value of the assets sold	185
Less : Loss on sale of assets	<u>(40)</u>
Proceeds on sale	<u>145</u>

### Assumption :

Interest income on investments ₹ 2,506 has been received during the year.

### Illustration 7

From the following Summary Cash Account of X Ltd. prepare Cash Flow Statement for the year ended 31st March, 2015 in accordance with AS 3 (Revised) using the direct method. The company does not have any cash equivalents.

#### Summary Cash Account for the year ended 31.3.2015

	₹ '000		₹ '000
Balance on 1.4.2014	50	Payment to Suppliers	2,000
Issue of Equity Shares	300	Purchase of Fixed Assets	200
Receipts from Customers	2,800	Overhead expense	200
Sale of Fixed Assets	100	Wages and Salaries	100
		Taxation	250
		Dividend	50
		Repayment of Bank Loan	300
		Balance on 31.3.2015	150
	<u>3,250</u>		<u>3,250</u>

### Solution

#### X Ltd.

#### Cash Flow Statement for the year ended 31st March, 2015 (Using direct method)

	₹ '000	₹ '000
<b>Cash flows from operating activities</b>		
Cash receipts from customers	2,800	
Cash payments to suppliers	(2,000)	
Cash paid to employees	(100)	
Cash payments for overheads	(200)	
Cash generated from operations	<u>500</u>	
Income tax paid	(250)	
Net cash generated from operating activities		250

**Cash flows from investing activities**

Payments for purchase of fixed assets	(200)	
Proceeds from sale of fixed assets	<u>100</u>	
<i>Net cash used in investing activities</i>		(100)

**Cash flows from financing activities**

Proceeds from issuance of equity shares	300	
Bank loan repaid	(300)	
Dividend paid	<u>(50)</u>	
<i>Net cash used in financing activities</i>		(50)
Net increase in cash		<u>100</u>
Cash at beginning of the period		<u>50</u>
Cash at end of the period		<u>150</u>

**Illustration 8**

Given below is the Statement of Profit and Loss of ABC Ltd. and relevant Balance Sheet information:

**Statement of Profit and Loss of ABC Ltd.  
for the year ended 31st March, 2015**

	₹ in lakhs
<i>Revenue:</i>	
Sales	4,150
Interest and dividend	100
Stock adjustment	<u>20</u>
Total (A)	<u>4,270</u>
<i>Expenditure:</i>	
Purchases	2,400
Wages and salaries	800
Other expenses	200
Interest	60
Depreciation	<u>100</u>
Total (B)	<u>3,560</u>
Profit before tax (A – B)	710
Tax provision	<u>200</u>
Profit after tax	510

## 2.78 Accounting

Balance of Profit and Loss account brought forward	<u>50</u>
Profit available for distribution (C)	<u>560</u>
Appropriations:	
Transfer to general reserve	200
Proposed dividend (including CDT)	<u>330</u>
Total (D)	<u>530</u>
Balance (C – D)	30

Relevant Balance Sheet information	31.3.2015	31.3.2014
	₹ in lakhs	₹ in lakhs
Trade receivables	400	250
Inventories	200	180
Trade payables	250	230
Outstanding wages	50	40
Outstanding expenses	20	10
Advance tax	195	180
Tax provision	200	180
Assessed tax liability		

Compute cash flow from operating activities using both direct and indirect method.

### Solution

#### By direct method

#### Computation of Cash Flow from Operating Activities

	₹ in lakhs	₹ in lakhs
Cash Receipts:		
Cash sales and collection from Trade receivables		
Sales + Opening Trade receivables – Closing Trade receivables (A)	4,150 + 250 – 400	<u>4,000</u>
Cash payments:		
Cash purchases & payment to Trade payables		
Purchases + Opening Trade payables – Closing Trade payables	2,400 + 230 – 250	2,380
Wages and salaries paid	800 + 40 – 50	790
Cash expenses	200 + 10 – 20	190

Taxes paid – Advance tax			<u>195</u>
(B)			<u>3,555</u>
Cash flow from operating activities (A – B)			<u>445</u>
<b>By indirect method</b>			
Profit before tax			710
Add: Non-cash items : Depreciation			100
Add: Interest : Financing cash outflow			60
Less: Interest and Dividend : Investment cash inflow			(100)
Less: Tax paid			(195)
Working capital adjustments			
Trade receivables	250–400	(150)	
Inventories	180–200	(20)	
Trade payables	250–230	20	
Outstanding wages	50–40	10	
Outstanding expenses	20–10	10	<u>(130)</u>
Cash flow from operating activities			<u>445</u>

**Illustration 9**

Prepare Cash flow for Gamma Ltd., for the year ending 31.3.2014 from the following information:

- (1) Sales for the year amounted to ₹135 crores out of which 60% was cash sales.
- (2) Purchases for the year amounted to ₹55 crores out of which credit purchase was 80%.
- (3) Administrative and selling expenses amounted to ₹18 crores and salary paid amounted to ₹22 crores.
- (4) The Company redeemed debentures of ₹20 crores at a premium of 10%. Debenture holders were issued equity shares of ₹15 crores towards redemption and the balance was paid in cash. Debenture interest paid during the year was ₹1.5 crores.
- (5) Dividend paid during the year amounted to ₹11.7 crores (including Dividend distribution tax) was also paid.
- (6) Investment costing ₹12 crores were sold at a profit of ₹2.4 crores.
- (7) ₹8 crores was paid towards income tax during the year.
- (8) A new plant costing ₹21 crores was purchased in part exchange of an old plant. The book value of the old plant was ₹12 crores but the vendor took over the old plant at a value of ₹10 crores only. The balance was paid in cash to the vendor.

## 2.80 Accounting

(9) The following balances are also provided:

	₹ in crores 1.4.2013	₹ in crores 31.3.2014
Debtors	45	50
Creditors	21	23
Bank	6	

**Answer**

**Gamma Ltd.**

**Cash Flow Statement for the year ended 31st March, 2014**

**(Using direct method)**

Particulars	₹ in crores	₹ in crores
Cash flows from operating activities		
Cash sales (60% of 135)	81	
Cash receipts from Debtors [45+ (135x40%) - 50]	49	
Cash purchases (20% of 55)	(11)	
Cash payments to suppliers [21+ (55x80%) - 23]	(42)	
Cash paid to employees	(22)	
Cash payments for overheads (Adm. and selling)	(18)	
Cash generated from operations	<u>37</u>	
Income tax paid	(8)	
Net cash generated from operating activities		29
Cash flows from investing activities		
Sale of investments (12+ 2.40)	14.4	
Payments for purchase of fixed assets	<u>(11)</u>	
Net cash used in investing activities		3.4
Cash flows from financing activities		
Redemption of debentures (22-15)	(7)	
Interest paid	(1.5)	
Dividend paid	<u>(11.7)</u>	
Net cash used in financing activities		<u>(20.2)</u>
Net increase in cash		12.2
Cash at beginning of the period		<u>6.0</u>
Cash at end of the period		<u>18.2</u>



### Summary

- Cash flow statement dealt under AS 3.
- Based on cash concept of profit.
- Benefits include providing information relating to changes in cash and cash equivalents of an enterprise.
- Useful tool of planning.
- Cash include :
  - (a) Cash in hand
  - (b) Demand deposits with banks
  - (c) Cash equivalents.
- Cash flow activities may be classified as inflow and outflow but as per AS-3 they are classified as Operating Activities, Investing activities, Financing activities.
- Operating activities are principal revenue generating activities.
- Investing Activities relate to acquisition and disposal of long-term assets and other investments.
- Financing Activities include the ones which result in changes in the size and composition of the owner's capital (including preference share capital) and borrowings of the enterprise.
- Methods to calculate cash flow from operating activities include:
  - (a) Direct Method
  - (b) Indirect Method also known as reconciliation method.
- In order to calculate cash flow from investing activities inflows and outflows related to acquisition and disposal of assets, other than those related to operating activities, are shown under this category.
- In order to calculate cash flow from financing activities inflows and outflows related to the amount of capital and borrowings of the enterprise are shown under this head.